Accountancy

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Professional Notes

Ex Div

THE PROPOSED "STANDSTILL" ON ORDINARY SHARE DIVIDENDS CAME AS A RUDE shock, not only in itself, but also in the manner of its coming.

No one, whether supporter of the Government or not, avers that dividend control can have any real significance in directly checking the rise in money incomes. The most that is claimed for it is, in the words of the Chancellor of the Exchequer, that "the psychological consequences of sharp increases in dividends are far greater than the direct monetary consequences." That is to say, it is hoped that stabilised dividends will help to restrain workers in putting forward wage claims. Whether this indirect drag upon inflationary forces will materialise is open to grave question: it is even more doubtful whether any benefit of this kind that might possibly be derived is worth the cost. Among the items of cost to be brought into the reckoning are the damaging effects upon enterprise and saving, at a time when both are urgently required, and the paralysis of the new issue market in risk capital at a time when its machinery should have been allowed to run at its smoothest.

The untoward consequences of the projected control were enhanced by the uncertainties and ambiguities embalmed in the White Paper announcing it. There is little point in discussing these at the present stage, since if and when a Parliamentary Bill is forthcoming it will necessarily resolve many of them—and, as perplexed company officials and directors have already found, the Treasury is necessarily unable to anticipate the Bill by answering problems posed by the White Paper. Here is a conspicuous example of confusion resulting from the attempt to force *de facto* what is essentially a legalistic situation before it is defined *de jure*. If dividend control is eventually enacted, it will be in a Statute much more precisely and elaborately defined than Command Paper 8318 (which we reproduce on page 335 of this issue of ACCOUNTANCY). It is, indeed, a major constitutional issue whether the medium of the loosely worded Command Paper should be permitted to attempt the work of the nicely drafted and carefully debated Act of Parliament.

New Evidence on the Capital Shortage

A memorandum submitted by the *British Bankers' Association* to the Royal Commission on Taxation contains little that is new in the way of positive proposals. Mostly it reiterates the case against replacement cost depreciation. It brings to bear upon the argument, however, the results of an important statistical inquiry which the unique facilities of the banks have made possible. A sample of the accounts of some 1,500 private companies was exhaustively analysed to discover how far taxation had impeded capital formation. The investigation is particularly valuable because statistics of the finances of private companies are in the nature of things ordinarily even more inaccessible than those of public ones.

The finance becoming available to the companies during the period 1946 to 1949-50 was £54.6 million, made up as follows:

	£ million
Increased capital of shareholders	8.2
Additions to reserves from money profits	25.2
Increase in own capital resources	33.4
Decrease in cash and securities	4.6
Bank overdrafts	16.6
Deterioration in liquid position	21.2
Total finance available ..	54.6

There was an increase, described by the bankers as no more than reasonable in the circumstances of the time, of £45.7 million in stocks, and a net

decrease of £6.6 million in trade credit received, making a total of £52.3 million to be financed before any account was taken of increases in fixed assets. The finance shown as available was only £2.3 million in excess of this. It follows that if the companies added to their fixed assets more than this very small amount, which might well be insufficient even to preserve the fixed assets intact, this could have been done:

> only by incurring additional liabilities not shown . . . (e.g. by issuing loan capital) or by investing in the business sums required as specific provisions (e.g. in respect of tax liabilities). The experience of the banks does in fact show that sums held for payment of taxes are commonly used as working capital until paid over, when they have to be replaced by borrowing, probably from the banks.

The memorandum concluded that if inflation continues or if there is a trade recession, much of industry could only maintain its operations by looking to the banks for finance " on a scale which, in many instances, would not be justified in relation to the trader's own capital resources."

Among several incidental results of interest produced by the statistical inquiry is the conclusion that stock was turned over 6.5 times in 1946, but only 5.3 times in 1949-50. Does this perhaps indicate that the expansion of stocks during the period was, despite the bankers' assurance to the contrary, somewhat disproportionate ?

Protection for Shop and Other Tenants

To meet the situation that has arisen in many parts of the country as the result of the expiry of leases granted nearly a century ago, Parliament has passed the Leasehold (Temporary Provisions) Act, 1951. The new law came into force on June 24. At the same time an attempt has been made to kill two birds with one stone by giving relief also to shop tenants. This measure has been called a " standstill " measure, since it is intended to confer temporary protection for a limited period of two years, between June 24, 1951, and June 24, 1953.

Tenants who hold leases for upwards of 21 years are to be entitled to an automatic extension of their tenancies in certain cases. One important condition is that the tenant or a member of his family should be occupying some part of the premises as a dwelling upon the termination of the lease. Protection will be enjoyed not only where the lease expires within the two-year period but also where the lease has already expired before June 24, 1951. Where it has so expired there is the further condition that the benefit of the Act can be obtained only if any fresh arrangement made with the landlord after the expiry of the tenancy was on terms identical with those of the expired tenancy. One curious feature is that a tenant who has stayed in occupation after the expiry of his tenancy as a trespasser is put in a more favourable position than a tenant who has entered into a fresh tenancy, but on terms different from those on which he was previously holding the premises. The former is protected, the latter is not. The benefit conferred by the Act on tenants desirous of claiming its protection consists of an automatic continuation of the expired leases until June 24, 1953.

The position of shop tenants is dealt with somewhat differently, since, in their case, the tenancy will not be automatically renewed, and an application to the Court for that purpose will be necessary.

The benefit of the Act, moreover, can only be claimed where the tenancy expired or was terminated by notice to quit on June 24, 1951, but not on any earlier date, or where it will expire or be terminated some time during the two-year period. A renewal, if granted by the Court, cannot be for more than one year but successive applications for renewal may be made. In any case, a renewal may not prolong the tenancy beyond June 24, 1953.

Intestate Succession

The Committee on the Law of Intestate Succession (whose report has now been published as Command 8310, His Majesty's Stationery Office, price 9d. net) agreed unanimously that the fall in the value of money and the rise in the value of the matrimonial home had made inadequate the present rights of a surviving spouse, whether widow or widower, in the residuary estate. Statistics collected from a large number of recent wills showed that this was generally recognised, for, in estates up to £5,000, a high proportion of testators left the bulk of their property to the spouse. The Committee also felt that life interests in small estates are unsatisfactory. They recommended that, when there are surviving issue, the spouse should take, as well as the personal chattels, £5,000 free of estate duty and costs instead of the present £1,000. He or she should also retain the right to a life interest in half the remainder, but should have the option (exercisable within twelve months from the grant of representation) of claiming a capital sum in place of the life interest. Where there survive a parent or parents but no issue, the absolute interest of the spouse should be increased to £20,000 and half the remainder, the parents taking the other half. If the deceased leaves no parent but brothers or sisters (or their issue), the brothers and sisters should take the parent's share. In all these cases the spouse should have the option, exercisable within the same time, of buying at market value the deceased's interest in the matrimonial home, if the interest was freehold or a lease with more than two years to run. If there are no issue, parents, brothers or sisters, the spouse should take the whole estate. The same rules should apply to partial as to total intestacies. The Committee reject the suggestion that a mistress should be entitled to share in an intestate's property and they wish to confine the rights of illegitimate children to those already given by the Legitimacy Act, 1926.

The Committee had also to consider whether the provisions of the Inheritance (Family Provision) Act, 1938, should be extended to intestacies, that is to say, whether the Court should be given a discretionary power in particular cases of hardship to alter the rights given to the spouse and children by the general law. The Committee reported that a doubt had arisen whether the Act applied where there was a will but where no effective disposition had been made of some or all of the estate, and said that it should be made plain that the Act does so apply. The Committee recommended that the provisions of the Act should be extended to cover total intestacies. However sound the general law might be, there were bound to be hard cases; for instance, under the legislation proposed, if a wife who had married twice left £5,000, her widower would

take all and any children by her first marriage nothing.

The report is eminently sensible on all points and it is to be hoped that Parliamentary time will be found for making effective its recommendations.

"Accelerated Amortisation"

The powerful stimulus of "accelerated amortisation" is again being administered to American businesses working on defence contracts. The Defence Production Administration issues "certificates of necessity" stating the portion of emergency capital expenditure that can be written off over five years for pricing and tax purposes (although it has just announced that it will issue no more certificates for a moratorium period of at least sixty days). In fixing this portion, an estimate is made of the residual value of the assets at the end of the five years. This procedure is not so free and easy as that of the war years, when 100 per cent. of cost could usually be written off, sometimes during a period retractively telescoped into much less than five years. Also, it is being sharply criticised by some, who would allow accelerated amortisation as a charge against tax but not as a cost for price fixing, contending that the business man "gets it twice." As the American Institute of Accountants has pointed out in a vigorous reply, the contention is an utter absurdity. "Costs can be recovered only in prices."

The British business man fared worse, even during the war, with the exceptional depreciation provisions of the Excess Profits Tax, than the American is now doing, and to-day the Inland Revenue and Treasury are quite oblivious of any such phenomenon as "accelerated amortisation."

International Comparison of Income Taxes

The accompanying table, reproduced from the *Economic Survey of Europe in 1950* of the Economic Commission for Europe, shows that the level and progressiveness of income tax rates are broadly the same in the Scandinavian countries and the Netherlands as in the United Kingdom. In France and Italy the rates on the smaller and middle incomes are not much below those in the United Kingdom, though those on the larger incomes are lower. As the Commission points out, the differences in the totals of income tax collected are much greater than can be explained by differences in tax rates alone. In the United Kingdom, the Netherlands and Scandinavia some 10 per cent. to 12 per cent. of the national income is absorbed by the tax, but in France the proportion is $5\frac{1}{2}$ per cent. and in Italy only $3\frac{1}{2}$ per cent. These discrepancies point to the seriousness of tax evasion in France and Italy (and in Western Germany) since the war. The Commission rightly warns that the argument does not imply that tax evasion is absent in the other countries. But it adduces one piece of evidence that is hardly conclusive. The taxed profits of individuals and companies engaged in agriculture and horticulture in the United Kingdom were, the Commission states, about £125 million in 1947, whereas the official estimate of income from farming, conceptually not very different, was £205 million. We should think, however, that the difference between these two figures is in considerable degree due to under-assessments of farmers the annual value of whose land did not exceed £100, who were therefore taxed under Schedule B. Any under-assessments of this kind resulted not from tax evasion but from the system of not assessing these small farmers under Schedule D.

Solicitors' Accounts—Accountants' Certificates

A solicitor recently claimed that the rules regarding accountants' certificates did not apply to him because he had not held or received clients' money. He had endorsed cheques and drafts received by him without passing them through a bank account. Counsel has given the opinion, however, that the receipt of a cheque or draft is the receipt of money within the rules, that a solicitor is bound to keep books of account with reference to such money and that he must deliver an accountant's certificate under Section 1 of the Solicitors Act, 1941. The Council of the Law Society state that the precise manner in which transactions of this kind are recorded may vary, but they emphasise that the keeping of accounts in proper form and the making of accurate statements in declarations for practising accountants are responsibilities of solicitors and cannot be delegated to accountants.

EFFECTIVE RATE OF INCOME TAX FOR A MARRIED COUPLE WITH TWO CHILDREN

Percentages of family income

Country	Year	Income tax liability as a percentage of income before tax for family income amounting to: 3	4	5	7	10	15	20	25	30	40	50	100 times net national income per head of population	Total amount of income tax actually paid as per cent. of net national income
Norway (Oslo) ..	1949	12	15	18	25	31	37	42	45	48	55	58	70	14[a]
Netherlands ..	1949	8	12	15	21	26	33	38	42	46	50	54	63	12
United Kingdom	1949	9	14	18	23	27	37	43	48	52	59	63	78	11
Sweden (Stockholm)	1949	14	16	20	25	30	36	42	45	47	..	..	..	11
Denmark (Copenhgn)	1949	15	17	20	23	27	31	33	35	36	38	39	42	10
Finland (Helsinki)	1949	10	13	15	18	23	29	35	39	43	48	51	60	8-9
Austria	1950	6	9	11	17	23	30	33	36	37	38	40	44	7·5
Germany: west'n zones	1950	5	9	12	19	26	32	37	39	43	47	51	65	7
France	1950	14	18	21	23	26	30	32	35	37	42	44	53	5·5[b]
Italy	1951	..	..	19	21	23	26	27	28	30	32	33	38	3·5[a c]

NOTE.—The rates of income tax shown for different levels of income refer to central and local government taxes on earned income. The figures in the last column, showing the total amount of taxes paid, include, in addition to income tax proper, ordinary annual property taxes levied on persons. For Italy, where no unified system of income tax exists, the figures refer to the total of (*a*) the scheduled tax on entrepreneurial income (*b*) the general tax on personal income and (iii) the local tax on income of families.

[a] Includes an amount of income tax levied on corporations.

[b] Including the tax on wage bill.

[c] 1948-49. Not available

B

Starting Businesses in South Africa

The attractions which the Union of South Africa holds out for new business enterprise may be gauged from the number of new companies starting operations there. In 1951 there were more than 4,000 of these, according to an announcement by the Minister of Economic Affairs. Their capital aggregated some £60 million, and about £62 million was added to the capital of existing companies.

Business men and companies wishing to extend to the Union will find much useful information in a booklet produced for private circulation by the Standard Bank of South Africa, Ltd., 10, Clement's Lane, London, E.C.4. This is entitled *Business Organisation and Company Formation in the Union of South Africa*, and is now in its fourth edition.

The gross output of industry in the Union (excluding mining) has increased threefold during the last ten years. The tariff policy is framed not only to produce revenue but also to foster local industries. Preferential agreements exist with the United Kingdom and other parts of the British Commonwealth.

The Union Government and local authorities are disposed to encourage new business enterprise, and factory sites with railway sidings may often be purchased cheaply.

In some trades a licence must be taken out before business is begun. A list of these is given in the booklet, with the fees charged.

The Union of South Africa is within the sterling area. Traders and others are advised to study the regulations governing exchange control, import and export permits, and price control. Trade mark law is substantially the same as English law before 1938, but competent advice should be obtained. The cost of registering a trade mark in normal cases is about £14.

The booklet contains a useful summary of the principal provisions of the Companies Act, 1926 (as amended), with notes on private companies, subsidiaries, and foreign companies.

Information is given in the booklet on the various Union and provincial income taxes payable. (On pages 344-6 of this issue of ACCOUNTANCY we publish the first part of an article on these taxes.)

The non-resident shareholders' tax of 1s. 6d. in the £ is primarily a tax on dividends paid by public companies in the Union to shareholders not ordinarily resident or carrying on business in the Union. The undistributed profits tax was abolished in the 1951 Budget.

Double taxation agreements have been concluded with the United Kingdom and the United States of America.

Death duties comprise estate duty and succession duty. No estate duty is payable where the estate does not exceed £10,000. On an estate of £200,000 duty would be £66,367.

An abridged list of stamp duties is included in the booklet, with notes on labour and industrial conditions and on aliens' registration.

SHORTER NOTES

Increased National Insurance Contributions

Higher contributions are payable for National Insurance from October 1. Stamps at the new rates will be available at post offices from September 24. The increase in the rate for employed persons (Class 1) is 4d. for men and women over 18 and 2d. for boys and girls under that age; it is divided equally between employee and employer, making the new contributions as follows:

	Men		*Women*	
	Employees	*Employers*	*Employees*	*Employers*
Age	s. d.	s. d.	s. d.	s. d.
18 and over	5 1	4 4	4 0	3 5
Under 18	2 11½	2 6½	2 5	2 0

There are corresponding increases in the rates for self-employed (Class 2) and non-employed (Class 3). A leaflet (N.I.63) setting out the rates can be obtained from National Insurance offices and post offices.

Burroughs Acquire Third British Factory

A new factory, its third in Britain, is to be built by *Burroughs Adding Machine, Limited*, on the same estate at Strathleven, Scotland, as the factory opened by the company last year. It is announced that the new factory, which will be completed within eighteen months to two years, will produce some radically new machines, as well as those, ranging from small hand-operated machines to complex electrical accounting calculators, made at the two existing factories.

Higher Limits for Small Savings

Deposits in the Post Office and Trustee Savings Banks are to be allowed up to a maximum of £3,000 for a depositor, instead of £2,000. The limit on individual holdings of Defence Bonds will be £3,500, instead of £2,500. The new maximum for Defence Bonds is operative on October 1, but the date of the new limits for savings deposits is to be announced later.

Lectures in Accountancy at Cambridge

It is pleasing to note from the *Cambridge University Reporter* that among the lectures proposed by the Board of the Faculty of Economics and Politics for the year 1951-52 is a course on the Elements of Accounting, and that the lecturer is Mr. F. Sewell Bray, F.C.A., F.S.A.A., a member of the Council of the Society of Incorporated Accountants and of the Society's Research Committee.

Resale Price Maintenance—Special Cases

The Board of Trade invite trade associations and firms to let them have any evidence of exceptional features of particular industries which might cause a general ban on retail price maintenance to produce special difficulties. The Board is already in touch with associations representing traders in books, petrol, building materials and certain technical goods with which "after-sales" service is usually provided (for example, cars and radio sets), as the associations claim that the special circumstances of these trades would make the proposed ban unworkable. The Board adds that general arguments for or against resale price maintenance are not being sought.

Census of Production Results

The preliminary results of the Census of Production for 1948 are summarised in the *Board of Trade Journal* for August 11. The summary reproduces and totals all the figures which have been published separately for industrial groups during recent months. The grand totals show that 77,838 establishments, employing 7,792,912 operatives and 1,346,050 other staff produced a net output of £4,960.5 million in 1948. At the end of the year their stocks of finished goods and work-in-progress were valued at £1,048.5 million, and stocks of material and fuel at £1,020 million, being increases of £160.2 million and £136 million since the beginning of the year. Their investment in new plant and machinery amounted to £304.5 million during 1948, in new buildings £84.7 million and in new vehicles £23.3 million.

ACCOUNTANCY

FORMERLY THE INCORPORATED ACCOUNTANTS' JOURNAL ESTABLISHED 1889

The Annual Subscription to ACCOUNTANCY *is 17s. 6d., which includes postage to all parts of the world. The price of a single copy is 1s. 6d., postage extra. All communications to be addressed to the Editor, Incorporated Accountants' Hall, Temple Place, Victoria Embankment, London, W.C.2.*

Economists and Accountants

SOME SIX YEARS AGO THE INSTITUTE OF Chartered Accountants and the National Institute of Economic and Social Research, impressed by the need for a "closer understanding between accountants and economists regarding the principles applied in their respective fields of work," appointed a Joint Committee to further this good work. And now the report of the Committee is published, under the title *Some Accounting Terms and Concepts* (Cambridge University Press, 46 pages, 3s. net). We confess, with reluctance and with respect for the distinguished authors of both Institutes, that we read this booklet with disappointment that mounted from page one to page 46. Six years of consultations seem to have brought forth little more, beyond a useful discussion of accounting procedures, than the negative conclusion that never will either side be persuaded that it is other than a Stokes confronted with a Mossadiq.

For ourselves, we do not believe that the twin disciplines of accountancy and economics need stand so far apart—and we feel that the pressure of events will force them to draw closer together. Examining the numerous differences between them that are set out in the booklet, only two need be regarded as really important: the others are but marginal, and would soon disappear if the central differences were resolved. The one important difference is over the measurement of stock usage during the accounting period, the other is over the measurement of the consumption, during the period, of fixed assets. It is explained that economists, concerned with the maintenance of physical assets, would not strike the figure for the operating profit of a business before deducting from operating incomings sufficient to allow for both stock and fixed assets to be kept, in a physical sense, as they were at the beginning of the period. On the other hand, the accountants' criterion is described as the maintenance of the money capital of the proprietors, so that the deductions from operating incomings need suffice only to keep intact the money value of the stock and fixed assets.

In this accounting day and economic age, what we are here given is a rather bald statement of the differences of view. It is one which needs to be followed by a closely reasoned discussion of what feasible modifications to the "principles" of both economists and accountants would be neccessary for a *modus vivendi*. The report contains no discussion of this kind, does not even give arguments why neither side can make departures from the stand it is described as taking. If either economics or accountancy were founded upon rigid "principles" from which it would be sacrilegious to suggest any deviation, then, indeed, all that could be said is "Here is white—and there is black." But neither economics nor accountancy is divinely inspired. Both are pragmatic studies, to be fashioned by men in the service of men. Each can take on varying hues of greyness.

As an instance of what we have in mind, consider the economists' idea that fixed assets should be maintained intact in a physical sense. If this idea is carefully examined, it is seen to be neither precise nor quantitatively definable. And if it is not, then no economist can insist that depreciation should be just so much of replacement cost—can contend, Portia-like, that it should be not "more or less than a just pound." Again, in an incidental remark, the report itself says that what economists aim at maintaining intact is the "productive capacity of an enterprise." But, clearly, in a dynamic economy this is by no means the same thing as restoring the fixed assets to their original physical condition. There is scope for judgment in deciding how much money is needed to preserve productive capacity, and the figure finally hit upon need be only very remotely related to replacement cost. Or, again, it is argued by economists that the replacement cost basis of depreciation should be admitted for taxation purposes. But even if it were so admitted, what economist could conscientiously expect them to admit as an expense any part of a depreciation quota so calculated which, at the conclusion and in the end (as the Mexicans say), was not in fact turned into fixed assets in the business?

We think that on the side of accountants also there is a greater willingness to modify traditional procedures than is admitted in the report—or, at least, that there would be a greater willingness, if the case were properly argued. As an example, take the treatment of "inventory profit." The report allows, in a pregnant but tantalisingly laconic reference, that some methods of calculation of stock usage—"first in, last out," base stock—alternative to the most usual one, go part-way in applying the economists' principle of replacement cost. But they are described as "merely differences of method which do not affect the principles already outlined." Is this so? These alternative ways of computing stock usage might appropriately be regarded as aimed at achieving a profit figure considered to be more correct. Again, we suspect that there are many accountants who would be willing to follow Mr. Bertram Nelson in his suggestion (see ACCOUNTANCY for August, pages 297/8) that after providing for depreciation on historical cost, there should be an additional setting aside of operating incomings before computing distributable profit (perhaps in a separate account) and that this additional setting aside should be calculated upon lines which would be recommended for general adoption in the accountancy profession. The report could have given some guidance on what such lines might be, even without accepting the suggestion itself or one like it—but on this, as on so many other significant issues, it is silent.

Practical Problems of Incomplete Records—III*

VERY PRIVATE COMPANIES

By D. E. BOSTOCK-SMITH, A.C.A.

IN THEORY THE RECORDS OF PRIVATE LIMITED COMPANIES should never be incomplete. But in practice how often does the auditor find that the directors fail to present him with final accounts and a complete set of books?

This presents the first problem of the auditor of a private company; but he finds himself beset with many other difficulties. The directors frequently believe that accounts are required only for tax purposes; the auditor himself has to prepare the accounts which he is required to certify; information is often scanty; and the directors of "one-man" companies resent time spent by the auditor in verifying the figures.

The objection to unlimited vouching and verification is most difficult to counter. The difficulty arises because the objection is frequently well-founded, for the auditor is not liable to the whole world in respect of his activities. On the other hand the local bank manager may place considerable reliance on the figures, unbeknown to the auditor.

The auditor's first duty is to the shareholders. If he carries out that duty properly, no other person will suffer, in the absence of carefully concealed fraud. Creditors of a private company (other than the banks) rarely see the accounts. But the banks and the Inland Revenue are justified in assuming that a "clean" certificate implies that not only has the auditor given satisfaction to the shareholders, but he has complied with the requirements of the Companies Act. Irrespective of the limitations on an auditor's liability to third parties, the reputable practitioner prefers that his accounts should stand any reasonable test.

Where the directors are also the sole shareholders, they may seek to limit the functions of the auditor in order to reduce the cost of the audit. This attitude is not entirely unreasonable and needs careful consideration. The law does not state what procedure must be adopted by the auditor; he must use his own judgment in the circumstances of each case. If he is satisfied that a short cut will produce the same results as more conventional methods in a particular case, then he may choose the short cut. In fact, it is his *duty* to do so, rather than involve his client in unnecessary expense.

The law is most specific about the adequacy of the books. If these are inadequate, then the auditor must say so. No set of books can be complete—and in accordance with the requirement that they should indicate the assets and liabilities—unless the company maintains a private ledger, but in the dark recesses of the commercial world there are probably companies without such a ledger, in spite of the unqualified certificates on their balance sheets. It is difficult to decide where to draw the line. What constitutes the books of the company? If copy sales invoices are used as posting media can they be called day books? If so, can invoices inwards be collected together as part of the book-keeping system? If an invoice is part of a day book is a statement part of a ledger? The law is not concerned with trifles, and the auditor must take a stand which is based on common sense as well as on adherence to the rules.

The path can sometimes be smoothed by drawing the attention of the directors to the penalties in a liquidation where adequate records have not been maintained.

In one respect there is no room for any considerable deviation—in the form of the accounts. There is nothing to prevent an auditor from seeing that the form of the accounts complies with the requirements of the Act. He need not concern himself with esoteric arguments whether future taxation is a capital reserve, and whether investments are fixed or current assets—the remaining items will usually fall into their places after an intelligent study of the Act, or even a scrutiny of published accounts. *Careful presentation of the accounts frequently acts as a useful guide in determining the audit programme.*

Shareholders may come and go, but companies go on for ever, or until they are struck off the register. Present shareholders may be satisfied with the accounts, but the accounts belong to the company, and they might mislead future shareholders. Need the latter be considered? Providing the certificate is quite explicit about any deficiencies in the books or accounts, or the scope of the audit, the question need not arise. It is well known that the certificate must not only put the reader on guard, but it must give some indication of the reason for the auditor's apprehension.

Can the auditor limit his work and qualify the certificate indefinitely? Legally, there appears to be no objection. Nor is there any moral or professional obstacle to such a course if it is imposed on the auditor by a special circumstance. It may, in fact, be of greater advantage to the members that a qualified certificate should state the position frankly rather than that the accounts should fail to appear within a reasonable time. Nevertheless, recurrence of the circumstances should be unnecessary, and the auditor should not be satisfied with continually having to report unsatisfactorily on the accounts. He is justified in refusing to put his name to shoddy accounts, providing he is not being unreasonable.

* This is the third and last of a series of three articles. The first, on the Cash Account, was published in our July issue, page 253, and the second, on the Bank Account, in our August issue, page 303.

In small cases it is unwise to be arrogant. If the company is in the hands of one director who is, in effect, the proprietor, and he handles all the cash himself, the auditor may not regard it as reasonable to spend the proprietor's money on proving figures already fully understood by the proprietor. In such a case, surely the director can ask the auditor to avoid excessive work in that direction, even if the certificate has to be qualified. So far as the shareholders are concerned, *they have provided their own internal check.* The auditor can then rely on a typical *test* check.

The full paraphernalia of a first-class audit are designed to protect shareholders and creditors (but primarily shareholders) who can take no part in the business themselves. It is essential that unbiased persons should report to the shareholders that such matters as cash and stock, for example, are under proper control. Where in fact the shareholders are themselves exercising this control the nature of the audit may be adapted to meet the situation.

Consideration ought to be given to the possibility of evolving a statutory certificate for exempt private companies, which differs from the elaborate certificates at present in use.

Diverging for a moment from records which may be incomplete to others which should never be incomplete, one should not overlook the statutory books. The register of members tends to remain static, irrespective of transactions subsequent to the initial entries, until completion of annual returns demands action. The minute book is frequently ignored. Directors' remuneration is rarely noted, and it is fortunate for auditors that their tenure of office is no longer subject to official confirmation.

The widening scope of taxation has placed an increasing burden on all persons concerned with the accounts of small businesses. It is essential that the hundreds of thousands of small cases should not be hindered by regulations which are designed for large enterprises and are inappropriate to and uneconomical for the small business man.

(*Concluded*)

Points in Practice

OVERTRADING

THERE CAN BE BUT FEW ACCOUNTANTS who are not worried by the signs of overtrading in the accounts of some of their clients. It is the purpose of these notes to examine the causes and signs of this malady.

Definition

Overtrading may be described as endeavouring to maintain or expand trading with inadequate working capital, and particularly with a shortage of ready cash.

Causes

The most important general causes of overtrading at the present time are inflation, stockpiling, and high taxation. It is not proposed to deal with the specific causes which may lie in a particular financial policy pursued by the proprietors themselves.

INFLATION

In order to maintain production at a volume comparable with that maintained before the war, a manufacturer or trader is compelled to lock up in the assets of the business at least two or three times the amount of money needed in 1939. In some cases the multiplier is even larger.

This applies to both fixed and current assets, though a greater degree of attention has been focused on the inflated cost of replacing fixed assets than on the higher cost of carrying the same quantity of stocks as pre-war. But the full effect of the need for replacing fixed assets has probably not yet been felt, as the shortage of equipment means that many machines are being used long after their normal working life.

It is probable that inflated costs of replacing fixed assets have a more direct effect upon liquid resources than the inflation in the price of current assets, as the current asset/current liability ratio can remain reasonably constant in spite of rising prices. Even so there is a danger that among the current assets the items debtors and stock will expand at the expense of cash.

So long as increased paper profits can be retained in the business, it is possible to keep the real capital intact. Unfortunately the high rate of taxation is draining away these paper profits, and thus absorbing not only the real profits of the business but in effect the real capital as well.

Inflationary overtrading will undoubtedly be aggravated by the cancellation of initial allowances. For, although the relief obtained under the Income Tax Act, 1945, may have been a little belated in some cases, it did mean that financial assistance was obtained within a reasonable time of the incurring of the capital expenditure. Furthermore, the allowance was based upon the replacement cost of the plant or machine, and thus went some way towards offsetting the debilitating effects of wear and tear allowances based on historical costs.

STOCKPILING

Let us now turn to stockpiling. This is a word which has only recently assumed headline importance, but it is horribly descriptive. A scarcity of certain goods and raw materials has arisen through war scares, rearmament programmes, the ravages of the last war, the change in the balance of international power and so on. In the result, not only Governments but businesses too are hoarding goods which they anticipate will be in short supply. Businesses stockpile in these circumstances because if they are unable to obtain supplies at a later date they will be unable to employ their fixed assets fully, or to satisfy the requirements of their order book, apart from finding themselves in all probability confronted with even higher prices.

Thus by another process is the drain on working capital increased and overtrading as originally defined promoted.

SYMPTOMS

The seriousness of overtrading cannot be over-emphasised, and it is therefore proposed to review some of the more usual symptoms that indicate the onset of the malady. It is not suggested that the following symptoms are in order of importance:

1. A steady fall in the liquid resources though the gross profit percentage may remain steady.
2. When no new capital commitments have been entered into, an increase in loans or creditors without a corresponding increase in turnover.
3. Declines in the debtors/creditors ratio, and in the working capital ratio.

Unfortunately, these symptoms, whether present singly or more than one at a time, are often overlooked in the early stages, or wishful thinking puts forward an optimistic explanation of them, so that it is not until the *effects* are beginning to be felt that proper attention is paid to the " writing on the wall."

THE EFFECTS

From the foregoing remarks it is obvious that the main effect of overtrading will be shortage of ready cash. In the train of this shortage, however, come other disabilities.

1. Bad buying. — Normally it is cheaper to buy in bulk, but if money is short the suppliers may become difficult and deliver only small quantities against cash payment and at disadvantageous prices.

2. Wage difficulties.—In extreme cases cash becomes so short that the proprietors of the business start to worry on Monday about the source of the cash for the following Friday's wages!

3. Discounts.—Loss of discounts receivable through having to take extended credit, and loss through having to allow discounts larger than normal in order to attract early payment from debtors.

4. Increased expenses.—A reduction in profits through increased expenses, such as interest on bank loans raised to relieve the shortage of cash.

5. Inefficiency.—Loss through having to keep a staff of inferior quality, or one which is disgruntled at its wage rates. Inefficiency may also be caused through working with near-obsolete plant and machinery.

CONCLUSION

So far as the immediate problems of the accountant are concerned—apart from questions of national policy—it can only be suggested that he watches carefully for the fateful symptoms, and when they are observed (i) brings them to the attention of the proprietors or board of directors immediately, (ii) urges that panic buying is avoided and (iii) urges that cash resources are husbanded with the greatest care, even if it means the temporary curtailment of capital expenditure on a scheme of expansion.

Profit and Loss—II*

By BERTRAM NELSON, F.S.A.A.

A paper presented at the Incorporated Accountants' Conference, Dublin, June 14, 1951.

THE LEGAL DEFINITION OF PROFIT

In one of the best-known books on draftsmanship, the 1950 edition includes the following as a standard clause in a Service Agreement :—

" Within one month after each stocktaking, an account shall be prepared by the Employer showing the outgoings and receipts of the said business. The net profits of the said business shall be the difference between the gross takings as appearing from the said accounts and the outgoings."

It would be excellent if the legal and accountancy professions could collaborate in devising clauses which would be more in accordance with accounting practice, on an income and expenditure basis. " There is no single definition which will fit all cases " (*Bond* v. *Barrow Haematite Steel Company* (1922, 1 Ch.353 per Farweld, J.), but if definitions are to be attempted in legal agreements, better precedents could be devised. There are decisions which embody two different concepts of profits. " The word ' profit ' has a well-defined legal meaning. ' Profits ' implies a comparison between the state of a business at two specific dates, usually separated by an interim period of a year. The fundamental measure is the amount of gain made by the business during the year . . . ascertained by a comparison of the assets at the two dates " (*Re Spanish Prospecting Co.*,

* The first part of this paper was published in our August issue, pages 296-300.

Ltd. (1911, 1 Ch.92 C.A. per Fletcher Moulton, L.J.). "The word 'profit,' generally speaking, means the excess of returns over outlay" (*McClelland* v. *Hyde* (1942, N.I.I. per Babington, L.J.).

THE EFFECT OF PROFITS

Company earnings are an important factor in the national income, and company savings constitute a large part of total savings.

	1938	*1948*
Net savings by persons	£143 million	£6 million
Net savings by companies	£170 million	£545 million

The true computation of profit is necessary if resources are to be used in the best possible way: this is true of private enterprise and even more true of state enterprise.

It is satisfactory that so much of our accountancy procedure is already being used in the new technique of social accounts. While there is much to be said against standard forms of profit and loss accounts, it would be helpful if standard headings could be adopted so that collation may be possible. Some of the headings suggested by Mr. F. Sewell Bray in his *Social Accounts and the Business Enterprise Sector of the National Economy* are given in the Appendix.

Full use has not been made by accountants of the information which is available in Government publications, including in particular the Monthly Digest of Statistics and the Census of Production Reports. Useful comparisons could be made between the statistics of individual businesses and general trade movements.

INTERNATIONAL ASPECTS

The free movement of profits between countries is too broad a subject to discuss in a paper of this kind. It may, however, be of fundamental importance. There is possibly a case for a new kind of limited company—an international company with no national domicile. Its memorandum and articles of association could be framed under U.N.O. auspices; its profits would be taxed only once, in ratio to the activities carried on within each national boundary; its capital could be provided on an international basis and it would be free to use its profits where increased productivity was most needed. "We are living through the first world revolution. What we have long called 'the modern world' is coming to an end and we are beginning a new chapter in the history of human development. The change is so profound that there is no level of human experience which is untouched by it. If we grasp our situation in its entirety . . . we shall realise that it is full of hope and opportunity and that it moves towards a great emancipation. For its goal is the unification of the world in a common life." (*Conditions of Freedom.* John MacMurray.)

THE OPPORTUNITIES OF THE ACCOUNTANCY PROFESSION

In conclusion, a fundamental problem of the accountancy profession may be faced. That problem is well expressed in some sentences taken from a paper given at our Balliol College course last September by Mr. John Ryan:

"The financial accounts themselves are naturally fundamental in any organisation, but because the form of these accounts has always been dictated primarily by legal and Inland Revenue requirements, they have unfortunately only an incidental value in day-to-day management. During recent years, therefore, more and more people have become aware that other kinds of figures are needed—figures gathered for the express purpose of controlling and planning operations. Can the accountant be reasonably expected to meet this demand? The individual responsible will need to have certain qualifications. First of all he will need to be familiar with the precise significance of the symbols with which he deals. He must, in other words, know the business pretty intimately, both production and sales. Has the accountant the time and opportunity to acquire the knowledge? He must also be able to relate this knowledge to outside events, for no business operates in a vacuum. It is the job of the person who prepares information for the management to be able to relate statements of internal operations to external factors, and to do this he must draw widely on national and international statistical sources. Now plainly, in many small businesses, it is the accountant who will have to satisfy this requirement, for he will probably be the only person in a position to do so. But I think that in so doing, he will have to realise that he is not doing the job for which he has been trained—and that it will involve an approach which may in many ways run counter to his whole acquired mode of thought. In the large organisation, therefore, it may be desirable to seek another solution. The provision of information to management can only be successfully undertaken by someone thinking in general management terms and by someone with practical knowledge of the problems, plans, and objectives with which the management are concerned. We need for this job what, for want of a better term, I would call a 'business statistician.' I do not know whether, in the future, the accountants may seek to make this field their own. There are some signs that many accountants are aware of the possibilities and also aware of what is involved. I am not sure myself whether the two jobs can be combined, but I am sure that it certainly cannot be done without a complete reorientation of present accountancy training. Whether this is possible without detriment to present standards of financial accountancy is a question one must leave to the profession itself to decide. We must be careful that our financial control in the business does not gum itself *and us* in its own web. It is a tool of management and must, therefore, not merely be content to produce evidence and information, but to distil from it what it all means, to project forward its advice on what can happen to affect our business and to show us in clear and unmistakable form what is happening and to do it quickly. A new world of exciting adventure lies before you. Do not let yourselves stagnate in a routine atmosphere which worships form and ceremony more than dynamic action. No one has a better chance to be management's guide, philosopher and friend—accept your opportunity to the

full in both training and experience, and industrial prosperity will provide its own reward.".

APPENDIX I

BANK OVERDRAFTS OF SOME LARGE COMPANIES

Name of Company	*Amount of Overdraft*	*Date of Accounts*
Distributive Trades :		
1. Beecham Group, Ltd. ..	£1,265,498	March, 1950
2. Great Universal Stores, Ltd.	£7,230,900	March, 1950
Rubber and Allied Produce :		
3. Dunlop Rubber Co., Ltd.	£4,630,500	December, 1949
Electrical Engineering :		
4. English Electric Co., Ltd.	£4,249,000	December, 1950
General Engineering :		
5. Babcock & Wilcox, Ltd. ..	£1,566,907	December, 1949
Chemical :		
6. Imperial Chemical Industries, Ltd.	£5,359,000	December, 1949
Tobacco :		
7. Imperial Tobacco Co. (of G.B. & I.), Ltd. ..	£28,384,000	October, 1950
Wool :		
8. Patons & Baldwins, Ltd.	£2,536,500	April, 1950
9. Salts (Saltaire), Ltd. ..	£1,800,000	March, 1950
Miscellaneous :		
10. British Oxygen Co., Ltd...	£2,120,500	December, 1949

APPENDIX II

Extracts from Suggested Form of Business Enterprise Primary Accounting Return, Profit-and-Loss Account

(From *Social Accounts and the Business Enterprise Sector of the National Economy.* By F. Sewell Bray. Cambridge University Press).

A. Production :

I. Inventories at beginning of accounting period :

II. Inventories at close of accounting period :

III. Increase (—) or decrease (+) in inventories :

1. Raw materials
2. Consumable tools and/or sundry stores
3. Work in progress or process

IV. Inventory replacement provisions :

V. Purchases of goods and services :

Total

Proportional or variable	×
Semi-fixed or semi-variable	×
Fixed or standing	×
	×

VI. Indirect taxes :

1. Excise duty
2. Factory rates
3. Transport registration dues

VII. Wages and salaries :

1. Direct wages to operatives
2. Wages of foremen and supervisors
3. Motor-drivers' wages
4. Salaries of works managers, technical directors and their assistants

VIII. Contributions to social security funds :

Total

Proportional or variable	×
Semi-fixed or semi-variable	×
Fixed or standing	×
	×

IX. (i) Depreciation and obsolescence (original costs) :

1. Factory buildings
2. Plant and machinery
3. Transport equipment

(ii) Additional replacement provisions

X. Factory insurances :

B. Selling and Distribution :

V. Purchases of goods and services :

VI. Indirect taxes :

1. Purchase tax
2. Rates of warehouses, salesrooms, etc.
3. Transport registration dues

VII. Wages and salaries :

VIII. Contributions to social security funds :

IX. (i) Depreciation and obsolescence

(ii) Additional replacement provisions

C. Administration and Management :

I. Purchases of goods and services :

II. Banks

Commission charges

III. Indirect taxes :

Rates of offices, etc.

IV. Salaries and fees :

V. Contributions to social security funds :

VI. (i) Depreciation and obsolescence (original costs)

(ii) Additional replacement provisions

VII. Insurances

D. Interest on Borrowed Money (before deduction of income tax)

Total payables

E. Operating Surplus

Total debits

Receivables

I. Net sales of goods and services

Less discounts allowed

II. Subsidies

(*Concluded*)

Control of Dividends

We reproduce, with permission of the Controller of H.M. Stationery Office, Command Paper No. 8318, entitled " Control of Dividends."

AS ANNOUNCED BY THE CHANCELLOR of the Exchequer on July 26, it is the intention of the Government to introduce, when Parliament reassembles in the autumn, a Bill providing for the control of dividends during a period of three years. The main features of this measure will be as follows:

(1) It will apply to every company registered under the Companies Act, 1948, or its predecessors, and to any company incorporated by Act of Parliament or Royal Charter.

(2) It will impose a limit on the gross amount* which may be distributed in dividends other than fixed-rate dividends.† The dividends to be controlled will include any participating element in preference dividends, cash bonuses, and other distributions not made by way of repayment of capital.

(3) In the case of an existing company the annual amount which may be distributed by way of controlled dividends will be (at the option of the company):

(*a*) the average of the amounts so distributed in respect of the last two accounting periods of the company for which, before July 27, 1951, a final dividend has been paid, or the decision or directors' recommendation as to a final dividend has been publicly announced (the amount for either period being adjusted proportionately in any case where there has been an alteration in the amount of the relevant capital between the end of that period and the end of the period for which the controlled dividend is paid);

or (*b*) Five per cent. of the relevant capital at the end of the period for which the controlled dividend is paid;

or (*c*) Ten thousand pounds.

An existing company means a company which has completed two such accounting periods as above-mentioned.

(4) In the case of a company other than an existing company as defined above, the annual amount which may be distributed by way of controlled dividends will be 7 per cent. of the relevant capital at the end of the period for which the controlled dividends are paid.

(5) (*a*) The permissible amount of dividend under the last two paragraphs for an accounting period other than a year will be proportionately greater or less, and similarly a proportionate adjustment will be made under paragraph 3 (*a*) above in the amount distributed for either of the two accounting periods there referred to where that period was greater or less than a year.

(*b*) The " relevant capital " for the purpose of calculating the permissible amount of dividend is the amount of the paid-up share capital other than capital carrying a right to a dividend at a fixed rate and other than capital paid up out of the company's assets since the beginning of the first of the two accounting periods referred to in paragraph 3 (*a*). Where the relevant capital at the end of any accounting period includes or included new capital not ranking for dividend during the period or part of it, the new capital or a proportionate part of it will be disregarded for that period.

(*c*) Subject to what follows in paragraph (7), a dividend will in every case be treated as paid for the accounting period ending last before the date of the distribution, except where it is expressed to be a dividend for the period in which the date of distribution falls. This will apply for calculating the dividends for the periods referred to in paragraph (3) (*a*) above, as well as dividends for later periods.

(6) In exceptional circumstances, the Treasury may decide that the amount of dividend permissible under paragraph 3 (*b*) or paragraph (4) above may be increased as they think fit.

(7) Measures will be taken to deal with attempts at forestalling and evasion. Thus where a company has announced but not declared a final dividend before July 27, 1951, it will not be allowed to obtain an increased standard under paragraph (3) (*a*) above by paying a higher dividend than that announced: any increase in the final dividend beyond the amount announced, and any extra dividend declared in addition to a final dividend for a period before July 27, 1951, will be treated as a dividend for the current period. Dividends for the current period which are distributed before the Bill passes will be taken into account, and if they exceed the permissible distribution for that period the excess in so far as declared after July 26, 1951, will be deductible from the permissible distribution for later periods. Measures will also be taken to deal with attempts to evade the effects of limitation for example, by repayment of capital, or by the conversion of ordinary capital into preference capital.

* The gross amount will be defined as for income tax purposes.

† A fixed-rate dividend means a dividend at a fixed rate on a share of any class payable in priority to all the dividends on some other class of share.

Index of Retail Prices

The present interim index of retail prices, which uses weights derived from pre-war consumption standards of manual wage-earners and non-manual salaried workers with not more than £250 a year, is admittedly unsatisfactory, says the Cost of Living Advisory Committee in a recent report (Command 8328, price 6d. net). Its recommendation for a new inquiry into family budgets has been accepted by the Government. The Committee rejects the suggestion of separate indices for different income groups and different areas. New weights will be assessed from the results of the inquiry for households with about £150 to about £1,000 a year, but the opportunity will also be taken to investigate spending habits of households outside this range. Unfortunately, it will take about two years before the inquiry is completed, but the Committee is now considering temporary improvements in the present index.

Tax Evasion in U.S.A.

A report by economists recently published by the *Twentieth Century Fund* in U.S.A. estimates that if the tax laws were more rigorously enforced, some $1,000 million (£360 million) a year could be added to the yield, for an addition of less than $10 million (£3.6 million) in costs of administration.

Leaves from the Notebook of a Professional Accountant

The Taxability of Casual Receipts

By ERNEST EVAN SPICER, F.C.A.

Foreword

SOME OF OUR READERS MAY HAVE GATHERED FROM CHANCE remarks which, from time to time, have fallen from our pen, that as between the Rev. Stephen Collins and Mr. Charles Greatheart there existed but little of that fellowship, which normally binds the Pastoral Shepherd to the individual members of his flock.

We cannot disguise the fact that the estrangement existing between these gentlemen originated out of some very unfortunate remarks made by Mr. Greatheart on the very subject which we have chosen for our immediate consideration and thus it behoves us to exercise the utmost restraint, in dealing with our theme, to avoid any charge of needlessly pouring oil on the glowing embers.

That the unkind words uttered by Mr. Greatheart still rankle in the soul of Mr. Collins is abundantly demonstrated by his action in removing from the vicarage library Mr. Bunyan's admirable treatise on *The Pilgrim's Progress*.

IT IS A VERY CURIOUS FACT THAT THE TERM "CASUAL receipt" conveys to the average man in the street a significance diametrically opposed to that which it conveys to an official of the Inland Revenue.

The gentleman in the railway carriage who dilates so learnedly on the rules and regulations governing income tax invariably assures his fellow travellers that casual receipts are immune from taxation, and never hesitates to support his argument by quoting actual cases which have come within his own experience. The Revenue official, on the other hand, invariably assures those who question him on the subject that casual receipts are normally subject to taxation, although when it comes to dealing with specific cases, he may be forced to admit some doubt as to whether they are properly assessable under Case I or Case VI of Schedule D.

It is clear that these two conflicting opinions cannot be reconciled as they stand, but nevertheless, if our talkative friend of the railway carriage would permit us to add just one single word to his statement, not only we, but every official of the Revenue would unhesitatingly accept his assurance. If he had said that some casual receipts were immune from taxation, he would have been right, but by suggesting that all such receipts were immune, he was unquestionably wrong. Conversely, the Revenue official, by his use of the qualifying word "normally," was right, whereas, if he had omitted this one word, he also would undoubtedly have been wrong.

We thus reach the somewhat unsatisfactory conclusion that while sometimes casual receipts are legally immune from taxation, they are more frequently assessable to tax.

It will be our endeavour to lay down some complicated rules and principles (which, fortunately, the man in the street will not understand) to guide us in reaching a decision as to whether any particular receipt of a casual nature is, or is not, legally assessable. The fact that some crony of the man in the railway carriage was not assessed in respect of certain casual receipts which had come his way is, of course, beside the point. In all probability, the facts were never brought to the attention of the authorities, who were thus deprived of the opportunity of showing what they could do when they really tried.

Before troubling about rules and principles, however, let us first deal with a case from Mr. Greatheart's notebook, which illustrates the truth of the old war-time warning that:

Loose talking in the railway carriage may assist the enemy.

ILLUSTRATION ONE

In the year 1938 Mr. Greatheart rented a furnished house in Angmering, on the Sussex coast, and regularly each morning caught the 9.6 a.m. express to London.

He did his utmost to avoid travelling in the same compartment with a certain Mr. John Pontifex, who loved the sound of his own voice and who was always anxious to instruct his fellow passengers on every conceivable subject, ranging from the growing of asparagus to the rotational instability of the giant stars.

Notwithstanding his efforts, Mr. Greatheart often found himself facing this gentleman in the railway carriage, and in consequence was forced, willy-nilly, to listen to long dissertations which were addressed to no individual in particular, but rather to the occupants of the carriage in general.

Now it happened, one morning, that an elderly gentleman, who was seated next to Mr. Greatheart, remarked casually, after glancing at the financial columns of *The Times*, that Stock Exchange speculation was, in his opinion, the safest method so far invented of losing money. This opening proved more than sufficient for Mr. Pontifex, who forthwith proceeded to describe how a small annual fortune could be made, without the least risk of loss or liability to tax, by the purchase and subsequent sale of suitable dwelling houses situated in popular seaside resorts. He further informed his listeners that his friend, Mr. George Pilcher, who at present resided at No. 17, Ridgeway Avenue, had done this successfully for several years. He added that he knew for a fact that Mr. Pilcher had made a very substantial profit in the year 1935 by purchasing a

fairly large house at Westgate-on-Sea and converting it into two separate dwellings (one of which he had occupied for a short period pending sale) and that in the following year, 1936, he had made nearly £3,000 net profit on the purchase and sale of a hotel at Whitby on the Yorkshire coast.

Ten days later, Mr. Pilcher received (by a curious coincidence) a polite letter from H.M. Inspector of Taxes, informing him that it had been reported to the Inland Revenue authorities that he had had considerable dealings in landed property during the past few years and requesting detailed particulars at his early convenience. He added that an interview might materially assist matters.

By an almost equally curious coincidence, after the lapse of a further eight days, Mr. Greatheart received the following letter from Mr. George Pilcher.

17, Ridgeway Avenue,
Angmering.

Charles Greatheart, Esq. August 22, 1938.

DEAR SIR,

I have been advised by my friend, Sir Ambrose Whiting, to consult you on an important taxation problem, which is causing me some anxiety.

I should be greatly obliged if you would name a date and time convenient to yourself, when I could call on you.

Yours faithfully,

GEORGE PILCHER.

Mr. Pilcher's reaction to Mr. Greatheart's account of what had been said in the railway carriage proved typical of the man.

While blaming Mr. Pontifex for discussing his private affairs in public, more particularly as he had rewarded that gentleman very generously for assisting him to find suitable properties, he stated that if—notwithstanding the assurances which he had received—he was, in fact, liable to tax on these "casual receipts," as an honest citizen he would naturally wish to pay his just dues. On the other hand, if Mr. Pontifex were right in stating that they were immune from all taxation, he would resist the claim by all means within his power. He was anxious, however, to be guided by Mr. Greatheart and would unhesitatingly act in accordance with his advice.

Mr. Greatheart expressed the view that while a profit realised as the result of an isolated transaction of this nature would not normally attract tax, a series of such transactions would almost certainly be held to constitute a trade, the profits of which would be assessable under Case I.

He suggested that an appeal to the Commissioners could do no harm, but, unless learned Counsel strongly advised to the contrary, he could not recommend further action. This advice was accepted and in due course an appeal was made to the General Commissioners.

Mr. Stapleton, of the Inner Temple, who was briefed by Mr. Crawley to conduct the appeal, drew the attention of the Commissioners very particularly to the fact that Mr. Pilcher had occupied two of the houses prior to sale and argued that this clearly demonstrated an intention to establish a residence rather than to realise a capital profit. Notwithstanding all his eloquence, however, the Commissioners held that the surpluses on all the sales, less the loss which had been sustained on the sale of a bungalow in the year 1937, were trading profits, properly assessable under Case I of Schedule D.

At a subsequent conference in Mr. Stapleton's chambers, it was decided that to take the matter to the Courts on a point of law would merely result in adding materially to the costs, and in consequence Mr. Greatheart was instructed to make the best bargain possible with the Inspector of Taxes.

A reasonable settlement was eventually reached, it being agreed that the "trade" had commenced on January 1, 1934. The adjusted profits of the four calendar years ending December 31, 1937, resulting in assessments for the fiscal years 1933-34 to 1938-39 inclusive, were as follows:

Calendar Year	*Adjusted Profit*	*Fiscal Year*	*Assessment*
	£		£
1934	320	1933-34	80
1935	3,680	1934-35	320
1936	2,860	1935-36	320
1937	460	1936-37	3,680
		1937-38	2,810
		1938-39	460

Mr. Pilcher was so impressed by Mr. Greatheart's tactful handling of this case that he requested him to deal in future with all his financial interests, including the audit of his stockbroking business (G. Pilcher & Co.), of which he was the sole proprietor.

Note.—It is satisfactory to record that Mr. Pontifex was assessed under Case VI in respect of the "casual receipts" which had been paid to him yearly by Mr. Pilcher.

There was an interesting sequel to this case, which afforded Mr. Pilcher unbounded satisfaction. Even the Inspector of Taxes, who was born in Glasgow, saw the joke and replied to Mr. Greatheart's leg-pull by quoting *Hamlet:*

Let it work;
For 'tis the sport to have the enginer
Hoist with his own petar.

We must not, however, fall into the evil habit of telling our tale backwards, so let us start all over again from the middle.

Mr. Pilcher had a very sound, but not a very extensive Stock Exchange business. Most of his clients nevertheless were men of substance; during the war years his profits soared and he found himself liable to pay considerable sums each year by way of excess profits tax.

By a lucky chance his "standard" was based on the profit of the calendar year 1935, in which year, it will be remembered, he had made his record profit of £3,680 as a "dealer" in house property.

Now, at the time when Mr. Greatheart reached a settlement with the Inland Revenue authorities in the year 1938, Mr. Pilcher had six unsold houses on hand, one at Eastbourne, one at Angmering and four on the Welsh coast, and at first he was inclined to sell them at whatever price they would realise and close down a "business" which, in reality, was not and never had been anything more than a hobby. Mr. Greatheart, however, advised otherwise, pointing out that there was very little sense in

destroying a profitable hobby merely because the Revenue authorities claimed a moiety of the spoils. He urged him, therefore, to continue in a quiet way, as if nothing had arisen to disturb the tranquil waters; to confine his attention to small house property and to avoid at all costs being tempted to dabble a second time in hotel properties.

Mr. Pilcher smilingly acknowledged the rebuke and early in the year 1939 sold the house at Eastbourne at a reasonable profit to Mr. Pontifex, who, for reasons best known to himself, was desirous of quitting the locality of Angmering.

In the year 1940 he sold one of the houses on the Welsh coast to his aged mother, who wished to sleep quietly in her bed and not be disturbed by air raid warnings. This was certainly not an arm's-length sale, but, nevertheless, it showed a small surplus over the original cost price, and four years later, he had the satisfaction of learning that his mother had sold this house at a price which assured to her a non-taxable "casual receipt" of £2,846.

Between the years 1941 and 1946 he was able to oblige several other relatives and friends who were house-hunting, but in no case did he sustain a loss.

The following table shows, in summarised form, particulars of Mr. Pilcher's activities as a dealer in real estate from the year 1938 onwards.

Calendar Year	*Adjusted Profit*	*Fiscal Year*	*Assessment*
	£		£
1938	630	1939-40	630
1939	220	1940-41	220
1940	20	1941-42	20
1941	180	1942-43	180
1942	330	1943-44	330
1943	40	1944-45	40
1944	120	1945-46	120
1945	70	1946-47	70

As Mr. Pilcher was carrying on two businesses simultaneously throughout the entire period during which Excess Profits Tax was in operation, Mr. Greatheart quite properly claimed that they must be treated as one for the purpose of this tax.

He was thus able to combine the standard profit of the stockbroking business, amounting to £3,840, with that of the real estate dealing business, amounting to £3,680, and so reduce the excess profits tax each year by a sum of £3,680, less the trifling annual profit on the dealing business. In this manner, Mr. Greatheart was able to show that not only had Mr. Pilcher made good the whole of the taxes which had been levied on his "casual receipts," but also that he had realised quite a substantial profit on the tax.

In addition he had brought joy to his aged mother's heart and profit to her purse, and had won the life-long gratitude of several friends and relatives.

All this—be it understood—had been accomplished by Mr. Pilcher, without lightening his own purse by the weight of one single copper farthing.

As that gentleman exclaimed, "Who would have thought it?" Quite so—but as Dr. Samuel Butler said in his imperishable poem of *Hudibras:*

> The fool can only see the skin:
> The wise man tries to peep therein.

Note.—During the war period, the martial appearance of Eastbourne struck such terror into the heart of Mr. Pontifex that he fled to Devonshire after selling his house at a loss of £860.

He was no more lucky in the south-west than he had been in the south-east; in fact, less so, for he was bombed out of his hotel on the very night after his arrival in Torquay.

We now turn to a consideration of the taxability of casual receipts, resulting from the purchase and sale of stocks and shares and other similar forms of amusement.

Can it be said that an individual, who periodically indulges in a mild flutter in the hope of realising a quick profit, is engaged in a trade, adventure or concern in the nature of trade?

Theoretically it depends on the number of the transactions, although in practice the degree of success may prove a determining factor. There is no law which says that such profits are not taxable, and the decision as to whether or not, having regard to the facts, they should be attacked, rests entirely with the Revenue authorities. On the whole these trustees of the public exercise a wise discretion and usually turn a "blind eye" on the gambler, knowing full well that most people who speculate lose on net balance, even though some few may scrape home with a profit.

If, therefore, in the future, it be decided to attack all speculative transactions, it will be a political rather than an economic move. The power to assess individuals on such profits remains a powerful weapon in the hands of the authorities, since they can exercise it at any time they feel "so disposed."

It will be realised, of course, that if in any particular case the volume of such transactions be sufficient to cause the authorities to claim that a trade has been established, it is only the net excess of gains over losses that can be assessed. What is not so generally understood is that if a gambler in stocks and shares sustains substantial losses, he also can claim that a trade has been established, and if the volume of his transactions be sufficient, he will succeed. In these circumstances, he will be in a position to set the loss against his share of the profits of his legitimate business, if he has such a business, or, in any case, to make a claim under Section 34.

It is more perilous than playing roulette at Monte Carlo because the odds are weighted more heavily against the gambler. In the first place, the Government imposes a stamp duty of 2 per cent.; secondly, the jobber differentiates between his buying and selling price; thirdly, values react so rapidly to political news that most people "miss the market," and lastly the average man loses by being too greedy. Vanity prompts most people to boast of their isolated successes but very few men talk so loudly of their losses, and thus one hears more about the fortunate speculator than of his less fortunate brother.

We should not, however, on that account blind ourselves to realities. At any rate the Revenue authorities entertain no illusions on the matter and are thus very wise to "keep off the grass." Let it be remembered, however, that, by adopting this passive attitude, they do not surrender any of their legal rights. The "forceps" are always available if the tooth really needs drawing.

It may be laid down as a general proposition that an isolated transaction of purchase and sale—which is not connected with any existing trade or adventure in the nature of trade, does not normally constitute a " source " giving rise to assessable income. This accords with the ancient proverb first quoted by John Heywood in the early part of the sixteenth century that:

One swallow maketh not summer.

Thus, where a man lays in a stock of vintage wine and later sells it at a profit, such profit does not normally attract tax. There are, however, exceptions even to this " summer-swallow " rule, the most notable being that of *Rutledge* v. *C.I.R.*

Rutledge v. *C.I.R.*
The appellant in this case purchased a vast quantity of toilet paper which subsequently he sold at a substantial profit.

The learned Judge, after giving deep and grave consideration to the contention that the transaction was an isolated one, and that it was impossible to suppose that toilet paper could have been purchased with ulterior intent, held that the very magnitude of the transaction precluded the possibility of any intent other than that of sale. It was an adventure in the nature of trade and any profit arising therefrom was taxable under Case I.

Where the isolated transaction is connected with an existing trade, the profit arising therefrom may be deemed to form part of the normal profits of that trade and assessable as such.

It is essential, however, that the isolated transaction should have a fairly direct connection with the trade.

If this be not the case, it will not normally be assessable at all, unless in itself it be an adventure in the nature of trade.

The following cases illustrate the above remarks.

Beynon & Co., Ltd. v. *Ogg*
Beynon & Co., Ltd. were coal merchants and colliery selling agents and occasionally bought wagons as agents for colliery companies. On one occasion, however, they purchased a considerable number of wagons on their own account and sold them at a profit. This profit was held to arise from their trade and to be assessable with their normal trading profits.

McKinlay v. *Jenkins & Son, Ltd.*
Messrs. Jenkins & Son, Ltd., were marble importers and on one occasion, while awaiting a consignment of marble from Italy, sold at a profit of £6,707 Italian currency which they had previously bought with the object of paying for this marble. When later the marble was delivered, they again purchased Italian currency to pay for the consignment.

It was held that the profit of £6,707 on the original currency transaction was an appreciation in value of a temporary investment in Italian lire and was not a taxable receipt.

It will be observed that had Messrs. Jenkins & Son, Ltd., not sold the lire, but instead utilised this currency to pay for the marble, the profit on the consignment would have been increased by £6,707 and tax would have been payable thereon.

As it was, their trading profit was reduced, with a consequential reduction of tax, as a result of the increased cost of the lire which they were forced to buy to pay for the marble, and they were left with a tax-free profit on exchange of £6,707.

Where isolated transactions, which, by themselves, do not give rise to taxable profits, are repeatedly undertaken, they may form either a trade within Case I or a " source " of assessable profit under Case VI.

The case of *Pickford* v. *Quirke* provides a typical example of this.

Pickford v. *Quirke*
On four separate occasions the appellant helped to form a syndicate to buy up cotton shares, liquidate the company and then sell, at a profit, the underlying assets to a new company.

It was held that although each of these transactions, taken by itself, would not have constituted a taxable receipt, being of a capital nature, when viewed together as a whole they formed a trade, the profits of which were assessable under Case I.

It may be asked how it happens that so many of these cases dealing with casual receipts come to the notice of the Revenue authorities, since it is unlikely that the individual in question would voluntarily risk a " snap " decision by thrusting his head into the lion's mouth. In this connection it must be remembered that a Government Department has many sources of information, including the anonymous letter writer, who, more often than not, can be identified with a disgruntled clerk.

Inspectors of Taxes—in common with all sportsmen—dislike these underhand methods—but, nevertheless, they are bound to give consideration to all such communications in order to test how far, if at all, they are justified.

We choose from Mr. Greatheart's notebook a representative example of this class of case.

ILLUSTRATION TWO

Until his death in the year 1939, Mr. Charteris Whiting was the senior partner in the merchant banking firm of Whiting & Grimstock. Throughout his life he had been an enthusiastic philatelist and, being blessed with a long purse, was usually able to outbid all competitors at auctions, when rare specimens came on the market. He also obtained correspondingly large prices for duplicates which he no longer required for his collection.

Thus he was constantly buying and selling stamps and nobody but himself and Mr. Greatheart had the least idea whether he was indulging in an expensive hobby, or whether he had converted an interesting hobby into a profitable business.

Now, in the year 1936, Messrs. Whiting & Grimstock were shocked to learn that one of their managers had been acting in the capacity of an unlicensed bookmaker for the benefit (or otherwise) of the members of their staff, to say

nothing of outside clients, and had been using their organisation, including their telephones, in this nefarious business. As a result the manager was summarily dismissed and, within a fortnight, Mr. Charteris Whiting received a communication from the Revenue authorities, regarding his philatelic activities.

Mr. Greatheart was thereupon instructed to deal with the matter, which obviously arose following information supplied by the manager. He listened to what the Inspector had to say and admitted quite frankly that Mr. Whiting's operations were undoubtedly extensive, and could not, by any stretch of the imagination, be termed "isolated transactions." As a business man Mr. Whiting naturally endeavoured to realise the highest prices for the specimens which he desired to sell, and conversely he paid as little as possible for those which he sought to buy. He, Mr. Greatheart, was therefore inclined to agree with the "anonymous letter writer" that a "trade" had been established and enquired how far back the Revenue would desire to go. To this, the Inspector replied by enquiring what profit had been realised during the past few years. Mr. Greatheart, however, was not prepared to answer this question until agreement had been reached as to whether a "trade" had or had not been established. It was a question of principle rather than of profit, but he had been authorised by Mr. Whiting to say that he would abide absolutely by the Inspector's decision. He added that Mr. Whiting had kept an exact record of the price paid for every stamp which had—at any time—figured in his collection and he also had a detailed record of all specimens sold. It would thus be a very simple matter to furnish accounts which he, Mr. Greatheart, would certify as correct.

After some further discussion the Inspector stated that he would consider the matter and give his decision in due course. Eventually he wrote informing Mr. Greatheart that the Revenue did not intend to pursue the inquiry.

Three weeks later Mr. Greatheart happened to call on the Inspector in connection with another case and when they had finished their business talk, the Inspector asked—purely out of curiosity—whether it was really true that Mr. Whiting had succeeded in "foxing" the dealers to the extent of making a profit out of what was normally a very costly hobby.

Mr. Greatheart replied that while it was true a profit of nearly £18 had been realised in the year 1922, in all other years a loss, usually amounting to four figures, had been sustained. He added that on many occasions he had informed Mr. Whiting that doubtless he could establish the fact that he was, unsuccessfully, carrying on the business of a stamp dealer, but Mr. Whiting had always replied that unless the Revenue made the first move, it would be undignified for him to do so.

As he was leaving the office Mr. Greatheart remarked that this was a somewhat unusual case inasmuch as the "informer" had established a profitable "bookmaking" business, largely at the expense of the "informee" by improperly using the latter's organisation, and thus avoiding the burden of all office expenses. Moreover, he had paid no tax on the profits of this business and had left the office of Messrs. Whiting & Grimstock without troubling to settle with those members of the staff who had successfully backed "Fleetfoot," by "Footrest" out of "Fleet Rabbit," to win the Cesarewitch.

Note.—On his death Mr. Charteris Whiting bequeathed his immensely valuable stamp collection to the British Museum.

(*To be concluded*)

Fraud and Evasion

By J. W. WALKDEN, A.C.A., A.S.A.A.

THIS ARTICLE WILL BE CONCERNED WITH TAX FRAUD AND with the type of case which usually finds its way into the Special Enquiry Branch of the Inland Revenue. Evasion may, of course, be legal. Or it may be inadvertent. Or, again, it may arise from negligence. I am not concerned with these forms of evasion here, though much could be said about each. My concern is with the deliberate income tax "dodger" who has caused something of a stir in Press and Parliament recently.

What is, in effect, the Criminal Investigation Department of the Board of Inland Revenue is not called by such an uncompromising name. No—to spare the taxpayer's feelings it is known as the Special Enquiry Branch. The result is that the general offices of the Branch get innocent callers inquiring about everything from Purchase Tax to P.A.Y.E.—but never fraud!

The first step—and it is the first because it explains to a large extent the way the Inland Revenue go about things—is to consider the powers which can be used against a fraudulent taxpayer. These powers are far-reaching. I here give them as the Inland Revenue see them. There are, however, many doubtful points which have not been tested in the Courts, perhaps because of the taxpayer's dislike of publicity.

The powers in question can be broadly divided under three heads:

(*a*) Powers of discovery or of getting evidence.

(*b*) Powers of punishment.

(*c*) Power to mitigate—this is the key to the Inland Revenue practice and is, in some ways, peculiar to the income tax code.

I will deal with these three groups in order.

(a) Powers of discovery

Contrary to general belief, the Inland Revenue do not indulge in underhand snooping—and have not the power to do so. It is true that informers sometimes give useful information, but it is also true that the Inland Revenue act with caution : they realise as much as any one that these people are prompted by spite and are apt to invent or at least greatly exaggerate. Rewards are rarely granted to informers.

Before 1942 the main power, outside the normal duty imposed on taxpayers to make returns of income, etc., was that contained in Section 139 of the Income Tax Act, 1918. This Section empowers the General Commissioners (and *not*, it will be noted, the Inspector himself) to issue precepts for information when dealing with appeals. It is perhaps more powerful than it seems, for the onus of upsetting an assessment on appeal is on the taxpayer.

In 1942 there was a significant and very important extension to this power. It is contained in Section 35 of the Finance Act of that year, which for the first time gave the Inland Revenue the right to demand production of business records and possibly even private ones as well. Where the taxpayer refuses to submit accounts, or where the Inland Revenue are not satisfied with the accounts he does produce, they may demand by written notice that he shall make his books available. The appropriate part of the Section is worth quoting. The Board's notice may require him :

> to make available within such time as may be specified in the notice, for inspection by the surveyor or by any officer authorised by the Commissioners of Inland Revenue, all such books, accounts and documents in his possession or power as may be specified or described in the notice, being books, accounts and documents which contain information as to transactions of the trade, profession or vocation.

The Section also extended, in similar terms, the power of the General Commissioners. The extended powers of the General Commissioners have, however, been used on occasions since 1942 and have sometimes included such records as private bank pass books. It is still a doubtful point whether this is justified, unless proof is given that such private pass books do " contain information as to the transactions of the trade "—but that is, after all, a fairly wide way of putting it.

On the whole, the officers of the Inland Revenue usually get at least the information they are after without invoking these formal powers. Whether that is a tribute to their skill in browbeating the poor taxpayer or their tact in handling him is a point on which I am not giving an opinion ! As far as District Inspectors of Taxes are concerned, some seem to have the knack of asking just that awkward question which brings a back-duty case home to roost, whilst others ask all the wrong questions and miss the vital point.

(b) Powers of Punishment

" Powers of punishment " sound, and are in fact, rather grim. We can divide them into two. First, action in the Courts—either criminal or civil—outside the taxing Acts. Second, penalty proceedings under the taxing Acts.

Civil proceedings might be taken for damages for deceit which, in theory, would enable the Inland Revenue to recover as damages all duty lost through fraud, irrespective of time limits for assessment. This is, however, one of those possibilities which has never yet been tested. It is doubtful if it would succeed, because alternative statutory rights exist under the Income Tax Acts.

In any event, since the time limit has been abolished in fraud cases from 1936-37 onwards (by that 1942 Act once again) this possible course will be less and less attractive to the Inland Revenue as time goes on.

But criminal proceedings are a very different kettle of fish. Where they have a provable case, the Inland Revenue can take action at common law or under the Perjury Act on charges based on false returns or claims or on false accounts, or there might be charges for forgery on false invoices and the like. Or a conspiracy charge might be possible, though this would only arise if two or more individuals were involved in the same fraud. The Enquiry Branch have actually been successful on a conspiracy charge, which involved four directors of a company, where no false accounts had been submitted to the Inspector and no false return forms had been completed.

It was necessary only to prove a conspiracy to defraud and this was done from the books and vouchers and third party evidence. All four directors received terms of imprisonment. So the Inland Revenue do, on occasions, catch the taxpayer even before he has been successful in dodging tax !

Then there are the penalties, penal duties, forfeits and sur-charges with which the Income Tax Acts fairly bristle. Some of them have never been used, though they have been in existence as long as income tax itself. It is not necessary to deal with them all and I shall touch on the main ones only. For income tax the Inland Revenue rely mainly on the provisions of Section 30 and Section 107 of the Income Tax Act, 1918.

Section 30 applies to a false claim for allowances—at first sight a limited application. But Section 17 of the Finance Act, 1920, requires that, in making a claim, the taxpayer must render a return of income. So if the return of income is false the taxpayer is guilty of an offence " *in making a claim*," although the claim itself may be in order. Section 30 of the 1918 Act, therefore, applies to a return of income. It cannot be used, however, unless there has been wilful intent to deceive. Proceedings must be taken in the High Court and the penalty that the Court can impose is a fixed amount (not a maximum) of £20, plus treble tax on total income with no allowances (in addition to the tax itself).

The Section does not apply to the return of income of a company, for this return is made for purposes of assessment only and is not also a claim for allowances.

It is worthy of note that the Section provides for a forfeit of £500 from anyone who aids and abets a taxpayer to make a false claim.

Section 107 of the 1918 Act applies to a taxpayer who neglects, refuses or makes wilful delay in rendering a true and correct return for *assessment* purposes. It applies to a *false* return as well as to cases of negligence ; it is under this Section that a false return by a company falls. But if it is only a question of negligence the taxpayer can put the

matter right and under Section 140 no penalty would then arise. If the return was deliberately falsified, however, Section 140 would *not* let him out. Proceedings under this Section are either before the Commissioners or in the High Court. The penalty is £20 plus treble tax *after* allowances. Section 28 of the Finance Act, 1943, extended to E.P.T. and profits tax the provisions of Sections 107 and 140 of the 1918 Act, but the effect is not quite the same. For income tax, penalty proceedings in fraud cases are competent only if there has been a false return, whereas for E.P.T. and profits tax proceedings can be taken in certain circumstances on the basis of false *accounts*. In fraud cases, as already mentioned, there is now no time limit for assessments or penalty proceedings after 1936-37.

These two Sections of the 1918 Act, Sections 30 and 107, are the main sources of the strength of the Inland Revenue because, as is explained below, both Sections give power to mitigate.

The penal duty Sections 132 and 146 are used occasionally but, as it were, only incidentally. An example of their being used would be where fraudulent transactions had been undertaken through a third party who, though he had thereby assisted in producing false accounts, had not also been guilty of aiding and abetting in the completion of a false *return*.

So much for the powers of punishment. Now for what I earlier described as the key to the whole system—the power to mitigate—the third of the powers.

(*c*) *Power to Mitigate*

This power, bestowed under Section 222 of the 1918 Act, is a perfectly simple one. It enables the Inland Revenue to mitigate penalties at any time—even after judgment has been obtained. By itself it would not be far-reaching, but coupled with Sections 30 and 107 of the same Act it provides the statutory justification for the practice of making private settlements. In the great majority of fraud cases the settlement is indeed a private monetary one.

Before considering the procedure of the Enquiry Branch, one important point which affects the procedure must be mentioned. Section 34 of the 1942 Act—the Section which appears in the celebrated " White Paper "—makes it clear that statements made and documents produced by a taxpayer can be used by the Inland Revenue as evidence in either criminal or penalty proceedings even when they have told the taxpayer that they may make settlements and that they are influenced by full disclosure. Thus since 1942 the Inland Revenue have been able to prosecute even if there has been a complete disclosure, and they can use the evidence they have obtained in the course of the disclosure. In practice prosecutions of this kind are likely to be extremely rare.

Procedure—(1) The Initial Steps

Having dealt with the powers of the Inland Revenue and with their methods, let us examine how they go about things once they have got on to the track of the tax dodger. The first and essential point to observe is that the taxpayer is kept in suspense until the very day of settlement. He does not know until that day whether he will be faced with a criminal charge in the Courts, whether there will be penalty proceedings, or whether he will be able to settle the whole thing discreetly by parting with a large sum of money. His advisers may be able to make a pretty shrewd guess, but even they will not know for certain what is going to happen. This is an extremely effective policy in enabling the Inland Revenue to be sure that they do get to the bottom of his tax " wangles." But its main justification is that it is necessary for the preservation of the rights of the Inland Revenue. Once they make it clear that they are prepared to settle, their right to prosecute is immediately prejudiced. This is the effect of Section 34 of the Finance Act, 1942.

The first thing that happens in an Enquiry Branch case is that the taxpayer receives a short letter inviting him to the Enquiry Branch. Surprisingly, perhaps, he nearly always accepts the invitation. At the interview he is told—I am putting the matter in quite general terms—that there is reason to believe that his accounts or returns are wrong, and that while no accusations are made, it is desirable that he should know the legal position in cases of fraud or evasion of tax. He is then handed a copy of the White Paper, which contains a copy of Section 34, and it may even be read over to him. It is explained to him that the Board can prosecute, or take penalty proceedings or make a settlement, and that in deciding what to do they are influenced by a full disclosure and by full facilities being provided for investigation. Finally, he is given a typed list of four or five questions and asked to reply in writing, after being warned not to be in too much of a hurry to answer on the spur of the moment.

The technique of putting this across, skilfully adapted to suit the nerves of each particular taxpayer, very often results in a disclosure, even though no promises are made by the Inland Revenue. The questions are straightforward, asking whether accounts and returns have been correct and whether access will be given to books, and so on. To a certain extent the whole procedure may appear a kind of " legalised blackmail," and it requires very strong nerves to refuse to answer questions, to resist the Inland Revenue throughout and to challenge them to do their worst. Some taxpayers start by being defiant, but break down later when presented with proofs of fraud based on facts obtained from their own books. I might mention in passing that the Enquiry Branch very rarely mistake their man and the entirely innocent taxpayer is a rarity indeed among the many who have dealings with the Branch. Another thing—the information on which the Branch acts is never disclosed. If it were, the taxpayer would know how much to disclose and how much to try to keep hidden.

But to revert to the questions. In his answers the taxpayer may admit there is something wrong, or he may not. In either event he is usually invited to the Enquiry Branch again. If he has made an admission he is asked to instruct an accountant to make an investigation, at his own expense, in order that a detailed disclosure can be made. The Enquiry Branch favour an entirely independent accountant, not the taxpayer's own accountant. This may happen even when the taxpayer has not made a disclosure, though it is then more usual for the Inland Revenue to make the

investigation, at least up to the point where the taxpayer is faced by the Inland Revenue officers with evidence compelling him to make admissions, when the independent accountant may come in.

To digress a moment, I might mention here that there was once a taxpayer who denied any irregularities and was so over-confident that he was quite willing to instruct an investigating accountant of the Inspector's choosing, in spite of his denials. He even went so far as to lay a bet with this accountant that he would pay him £5 for every 1d. of irregularities which he discovered. The Inspector had, of course, picked the accountant with care and knew he would do a good job. He did. He brought to light omitted sales of some £30,000. The Inspector obtained a good settlement but the taxpayer's bet with the accountant, needless to say, was not honoured !

Procedure—(2) The Accountant's or other Investigation

The investigating accountant, having completed his job, makes his report, which the Revenue officers usually asks the taxpayer to sign as representing his complete disclosure. They may also require him to sign a very comprehensive certificate of disclosure. They then proceed to make a thorough check of the accountant's figures. Both in making their own investigations and in checking the results of an accountant's, they aim to test in two ways the completeness of the disclosure. One is by exhaustive investigation of the business books, supported by test checks with information obtained from suppliers, customers, etc. The other is by building up comprehensive private assets statements, supported by annual income and expenditure accounts and private cash accounts. The first of these two methods is not always possible—records may have been destroyed—but the second is *always* used and, provided that all the assets (including bank notes) are brought to light, it is reasonably accurate.

Procedure—(3) The Sequel

Once the Branch has made its check, and omissions have been agreed and tax computed, the important matter of settlement arises—if all is well and no proceedings are contemplated. Most cases are settled without proceedings even when there may have been less than full disclosure. Much depends on the seriousness of the fraud, the extent of the penalty rights of the Inland Revenue, the degree of disclosure and co-operation by the taxpayer, and so forth. The penalty loading exacted by the Inland Revenue is usually based on the tax evaded by fraud. Their loading varies enormously. In cases of real financial difficulty it might be negligible, but in the more or less normal case it could be anything from 50 per cent. to 200 per cent. So it will be seen that full disclosure and full co-operation can make a vast difference when it comes to the final settlement, quite apart from whether or not there will be proceedings. It will be realised, however, that this penalty loading, plus any tax out of date for assessment, cannot exceed the penalties which the Inland Revenue can legally exact. In view of the severity of the penalty sections this is not often a limiting factor.

The trouble is that so many taxpayers make a partial disclosure in the vain hope that they will get away with the rest. An Inspector had a case of three brothers—scrap merchants—who made a disclosure and instructed an accountant to make an investigation. He did not have all the co-operation he desired and was not altogether happy about it, but made his report showing omitted sales of some £14,000. The Inspector knew there were more undisclosed sales and did his best to shake the brothers into admitting this before they signed the accountant's report—but without success. Ultimately, when the Revenue investigation was complete, the omitted sales proved to be more than £30,000, instead of £14,000, and all three brothers were charged with criminal offences, to which their Counsel advised them to plead guilty. Facing a penalty loading of 100 per cent. or more would have been a terrible blow to them and I think perhaps they preferred a term in gaol. In this they may succeed, for the Inland Revenue do not take proceedings for penalties in addition to criminal proceedings, though there would not appear to be anything to stop their doing so. But that is another point not yet tested in the Courts.

SOME WORDS OF ADVICE

Let me finish with some words of advice.

To the taxpayer whose only form of crime is evading tax illegally—these are probably the majority among tax dodgers—the best course is undoubtedly full disclosure. However, the " spiv " and the black marketeer whose whole activities are shady and the " professional " criminal would probably not take kindly to this advice. It is perhaps worthy of mention here that the Enquiry Branch have been known to succeed against criminals on tax fraud charges where the police have failed.

To the investigating accountant :

(*a*) Always do your utmost to ensure a complete disclosure. From what has been said about penalty loading it will be realised how one's bargaining power can be fatally weakened at the settlement interview if the Revenue officers can point to any serious flaw in the disclosure. Count upon it that they will make the most of any such flaws.

(*b*) Remember also that the Revenue officers are specialists with wide experience, and have the backing of their own legal staff. Furthermore, the Investigating Officer, with whom you may have fared reasonably well, is not the only one to be faced at the settlement. He will be backed by his Group Leader, who has many settlement interviews behind him. Therefore, it is just as well to have all possible reinforcements on your side to make the forces a little more equal—and from the very start of the case.

(*c*) Finally, do make sure in each case that the private side is properly tied up. So many times further omissions have been discovered by the Inland Revenue simply by seeing to this. It is just as well to take a leaf from the book of the Enquiry Branch and to adopt the self-balancing method which they have evolved. It is in principle very simple—merely the application of double-entry principles to the building up of private assets and income and expenditure statements, starting from detailed annual bank accounts and cash accounts. In detailed application it is not always quite so simple to apply and much more could be said about it, but that would require another article.

I think it would be agreed that the officers of the Enquiry Branch have done a good job in the past with the minimum of disturbance to the honest taxpayer. However, the extension of powers in the 1942 Act has its dangers. The present practice of keeping the victim in suspense and playing on his fears of publicity could be abused. Its effect, as far as the individual Investigating Officer is concerned, is that he acts in settlement cases as prosecutor, judge and jury all in one. Such power could warp his judgment.

Thus, if and when the Inland Revenue make an all-out drive to catch up on tax evasion, vigilance in watching for any abuse of the present methods will be necessary. That time may not, in fact, be far ahead. A thorough sample test in three or four Tax Districts has just been made to give the Board some idea of the scale of evasion and the Department is not now quite so short as it was of trained Inspectors.

Income Tax in South Africa—I

OUTLINE OF THE INCOME TAX SYSTEM IN THE UNION

By DAVID SHAND, A.S.A.A., C.A.(S.A.)

Taxes are levied in the Union of South Africa on taxable income, which consists of gross income (not being income of a capital nature or from non-Union sources), less all amounts exempt from tax as specified in the Income Tax Act and less all deductions or expenses incurred in the production of the income.

In order to qualify for taxation, the income must be derived from a Union source. Income tax liability is therefore contracted not only by Union residents but also by a person or a company non-resident but deriving income from Union sources.

The taxes fall into two classifications:

(1) Union taxes, levied by the Union Government in accordance with the Income Tax Act No. 31 of 1941, as amended.

(2) Provincial taxes, levied by the Administration of each of the four Provinces, in terms of the relevant taxing ordinances.

Rates of Taxes

The Union taxes consist of normal tax and super tax, the rates of which are fixed annually by Parliament. Super tax is payable only by persons whose taxable incomes are in excess of £1,775. The rate for normal tax on incomes up to £16,000 is, in the case of a married person, 15d. for every £ of the taxable income, and, in the case of an unmarried person, 18d. for every £ in the taxable income, plus in each case one-thousandth of a penny for each £ of taxable income in excess of £1. Each £ of taxable income in excess of £16,000 bears tax at the flat rate of 47d. in the case of a married person and 50d. in the case of an unmarried person, plus in every case a 20 per cent. surcharge, after subtracting certain rebates which are allowed as deductions from the tax.

Illustration

On a taxable income of £2,000 the rate applicable by a married person would be 16.999d. in the £ and by an unmarried person 19.999d. in the £. On a taxable income of £19,000 the tax would be as follows: by a married person 30.999d. in the £ and by an unmarried person 33.999d. in the £ on the first £16,000 in both instances, and thereafter flat rates of 47d. and 50d. in the £ respectively on the balance of £3,000.

There is no differential rate of super tax based on marital status.

Dividends from public companies are also taxable in the hands of the recipients for super tax purposes. The rate on incomes up to £16,000 is 24d. plus one-four-hundredth of a penny in each £ of income subject to super tax in excess of £1 and a flat rate of 8s. 8d. for each £ of such income of £16,000, plus a surcharge of 20 per cent. after subtracting an abatement of £210 which is allowed after calculating super tax on the basis outlined. The abatement of £210 is in effect an adjustment to exempt income up to £1,775 from super tax, as the calculation would make super tax of £210 payable on the first £1,775 of the taxable income.

Rebates

Rebates are allowed as deductions from tax, calculated according to the rates referred to as follows:

Primary rebates of £31 for a married person and £22 for an unmarried person are allowed. Secondary rebates consist of:

(*a*) A rebate of £10 for each unmarried child or stepchild or legally adopted child who was alive during any portion of the tax year and was not or would not have been, had he/she lived, over the age of 18 years on June 30 of the tax year or over the age of 21 years, if wholly maintained by the taxpayer.

(*b*) A rebate of £2 10s. for every dependant towards whose maintenance the taxpayer contributed in cash or otherwise, during the twelve months ended June 30 of the tax year, not less than £30.

(*c*) A rebate of 1/3 for each £1 or part thereof of life assurance premiums, etc., paid during the twelve months ended June 30 of the tax year. The maximum rebate is £4 or £7 10s. depending on whether or not the taxpayer has been allowed a deduction from his income in respect of contributions to an approved pension fund.

Provincial Taxation

Provincial tax consists of

(*a*) Personal Tax

(*b*) Provincial Income Tax

(*c*) Provincial Companies Tax

Provincial tax is computed as a percentage on normal and/or super tax payable before the imposition of the 20 per cent. surcharge. An individual is liable for the tax of the Province in which he resides, whereas a company is liable in respect of each Province for Provincial Companies Tax on so much of its taxable income as is derived from that Province.

The taxes vary in the different Provinces and are set out below.

Provincial Personal Tax, 1951

CAPE PROVINCE

Married

Under £250—nil.

£250—£1 plus 2s. 6d. for every completed £10 over £250. Maximum—£5.

Unmarried

Under £150—nil.

£150—£2 plus 2s. 6d. for every completed £10 over £150. Maximum—£10.

NATAL

Married

	£	s.	d.
£150 and under		10	0
over £150 to £250	1	0	0
over £250 to £450	2	0	0
over £450	3	10	0

less abatement of £25 off income for each child under 18 years (maximum abatement £100).

Less rebate of 12½ per cent.

Unmarried

	£	s.	d.
£250 and under	1	10	0
over £250 to £450	3	0	0
over £450	5	0	0

Less rebate of 12½ per cent.

ORANGE FREE STATE

Married

£200 and under—£1 plus 2s. for every completed £10 over £100.

over £200—£1 11s. 3d. plus 3s. 3d. for every completed £10 over £100.

Maximum—£6 5s.

Unmarried

£200 and under—£1 plus 3s. for every completed £10 over £100.

over £200—£1 17s. 6d. plus 5s. for every completed £10 over £100.

Maximum—£9 7s. 6d.

TRANSVAAL

Married

Under £250—nil.

£250 and over—£1 plus 2s. 6d. for every completed £10 over £250.

Maximum—£7 10s.

Unmarried

Under £150—nil.

£150 and over—£1 10s. plus 2s. 6d. for every completed £10 over £150.

Maximum—£12 10s.

Provincial Income Tax, 1951

(Calculated on each completed 1s. of normal and/or super tax payable)

CAPE PROVINCE

Married and Unmarried

30 per cent. of first £6,000 of normal and/or super tax paid plus 20 per cent. on payment in excess of £6,000.

NATAL

Married and Unmarried

25 per cent. of normal and/or super tax paid (less rebate of 12½ per cent.).

ORANGE FREE STATE

Married

25 per cent. of normal and/or super tax paid.

Unmarried

40 per cent. of normal and/or super tax paid.

TRANSVAAL

Married

25 per cent. of 80 per cent. (= 20 per cent.) of normal tax paid and 30 per cent. of 80 per cent. (= 24 per cent.) of super tax paid.

Unmarried

32½ per cent. of 80 per cent. (= 26 per cent.) of normal tax paid and 37½ per cent. of 80 per cent. (= 30 per cent.) of super tax paid.

Non-Resident Shareholders' Tax

There is also a Non-resident Shareholders' Tax, which is a tax payable by persons not ordinarily resident or carrying on business in the Union and by holders of bearer scrip, whether resident within or outside the Union, on dividends declared in their favour by Union public companies. Tax is deducted at the source at the rate of 7½ per cent. of the gross dividend.

Definition of Private and Public Companies

Limited liability companies are classified as public and private.

A public company is defined in the Act. Any company which is not a public company automatically ranks as a private company. The definition of public and private company as formulated in the Income Tax Act does not correspond with the definition in the Companies Act. Broadly speaking, a public company is one whose shares of all classes are quoted on a recognised stock exchange or a company in which the public are substantially interested as shareholders in every class of the shares issued by the company. The majority of companies which are private companies in terms of the Companies Act would be classified as private companies under the Income Tax Act. Public companies pay normal tax at the rate of 4s. 6d. in the £. There is a rebate of £45 allowed. They do not pay super tax but the dividends declared by them are taxable in the hands of shareholders for super tax.

A private company does not pay normal and super tax itself (except in certain exceptional cases). The income or profits of the company is apportioned by the Receiver of Revenue among shareholders according to their rights to participate in the income or profits of the company. Thus, if X.Y.Z. (Pty.), Ltd. has a taxable income of £1,000 and A and B are shareholders holding 25 per cent. and 75 per cent. respectively of the issued share capital, the Receiver of Revenue will allocate £250 to A (i.e. 25 per cent. of £1,000) and £750 to B (i.e. 75 per cent. of £1,000). The amounts apportioned to A and B from X.Y.Z. (Pty.), Ltd. will be added to the respective incomes

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Illustration—Union and Provincial Taxes

If a married man with two children under the age of eighteen years earns £3,000 per annum, the normal and super tax payable is computed as follows:

Normal Tax

Rate of Tax, 15d. per £ plus $\frac{1}{1,000}$ d. for every £ in

taxable income in excess of £1 .. .. $= 15\text{d.} + \frac{3,000 - 1}{1,000} = 17.999\text{d.}$

	£ s. d.	£ s. d.	£ s. d.
Normal tax = 3,000 × 17.999d. =		224 19 9	
Less Rebates			
(*a*) Primary Rebate .. .. =	31 0 0		
(*b*) Secondary Rebate, 2 children at £10 each =	20 0 0		
		51 0 0	
		173 19 9	
Plus surcharge of 20 per cent. on £173 19 9 =		34 15 11	
			208 15 8

Super Tax

Rate of Tax = 24d. plus $\frac{1}{400}$ d. for every £ in super-

taxable income in excess of £1 .. .. = $24\text{d.} \frac{3,000 - 1}{400}\text{d.} = 31.4975\text{d.}$

	£ s. d.	£ s. d.
Super tax = 3,000 × 31.4975d. =	393 14 5	
Less abatement =	210 0 0	
	183 14 5	
Plus surcharge of 20 per cent. on £183 14 4 =	36 14 11	
		220 9 4
Total Normal and Super Tax payable =		£429 5 0

Provincial Taxes (Cape Province)

	£ s. d.	£ s. d.	£ s. d.
Personal tax (maximum)		5 0 0	
30 per cent. of normal and super tax (i.e. before the 20 per cent. surcharge is added) *viz.*	173 19 9		
	183 14 5		
30 per cent. (on basis of completed 1s.) of ..	357 14 2	= 107 6 2	
			112 6 2
Total Taxes Payable ..			£541 11 2

of A and B from other sources. If X.Y.Z. (Pty.), Ltd. has a supertaxable income, the amount by which the supertaxable income exceeds the taxable income is apportioned among shareholders for super tax purposes. An assessed loss of a company is not apportioned among shareholders but is retained in its hands for set-off against subsequent income of the company.

Provincial Companies' Tax

This tax is payable by a company and is based on taxable income derived from each Province. The rate varies in each Province and rates for the year ended June 30, 1951, are as follows:

PROVINCIAL COMPANIES' TAX, 1951

CAPE PROVINCE

9d. in £1 of taxable income from the Cape Province.

NATAL

1s. in £1 of taxable income from sources within Natal. Minimum £5. Rebate of 12½ per cent.

ORANGE FREE STATE

1s. in £1 of taxable income from sources within Orange Free State. Minimum £10.

TRANSVAAL

1s. in £1 of taxable income from sources within Transvaal. Minimum of £7 10s. Above excludes financial companies who are taxed as follows:

Public financial companies, 1s. per £1 of dividend distributed. Minimum £7 10s.

Private financial companies, 1s. of income subject to super tax. Minimum £7 10s.

NOTE.—In Natal, Orange Free State and Transvaal, private companies (with the exception of financial companies in the Transvaal) pay only minimum tax.

A private company is exempt from tax in respect of such portion of its taxable income as is apportioned to persons who are subject to Provincial Tax on the income so apportioned to them. If all the shareholders of a private company are persons, the private company will not pay Provincial Companies' Tax, as the individual shareholders will be assessed for Provincial Tax on the profits of the company which have been apportioned to them.

Private Companies' Levy

Private companies' levy is payable by all private companies (other than a private company all of the shares in which are held as at the specified date by one or more public companies). The object of this levy is to provide relief to shareholders to whom are apportioned the profits of the company, but no corresponding dividends may be declared by the company. The shareholder in ordinary circumstances would have to pay tax on income which he does not receive. Under this arrangement, the company pays the tax in part or in whole on behalf of the shareholder.

Assuming private company A has a supertaxable income of £2,000 and there are two shareholders, X and Y, who each hold 50 per cent. of the shares, A company pays private companies' levy of 4s. 6d. in the £ to the Receiver of Revenue, i.e. £450, and X and Y are each credited with £225 by the Receiver of Revenue. In assessing X and Y personally, the Receiver of Revenue will allocate the supertaxable income of A company, namely £2,000, between X and Y, i.e. £1,000 will be added to each one's income from other sources. The resulting tax payable will be reduced by the credit of 4s. 6d. in the £.

If the taxes payable by X and Y in respect of their individual incomes amount to less than 4s. 6d. in the £, they will each receive a refund from the Receiver of Revenue for the difference.

(To be continued)

The Integration of Income Tax and Social Security*

The Inland Revenue Memorandum

THE MEMORANDUM SUBMITTED TO THE Royal Commission by the Board of Inland Revenue, which, as mentioned in our last issue, was shown to witnesses at the meetings of the Royal Commission on June 21 and 22, has since been made more generally available. It is entitled *The Liberal Party Scheme for the Reform of Income Tax and Social Security*, but it summarises and comments on the other similar schemes. These were proposed at various dates by Lady Rhys Williams, D.B.E., Messrs. Haynes and Kirton (actuaries), *The Economist*, Mr. S. P. Chambers, C.B., C.I.E., and Professor James Meade, C.B.

The memorandum says that the general argument underlying these schemes is that the income tax personal allowances are equivalent to social security payments but are granted only to tax-payers and vary according to their income: these payments exist side by side with the cash social security payments which are given to all who are unemployed, sick or retired and are fixed in amount. Moreover, the argument continues, two kinds of tax are, in effect, levied: a poll tax (the national insurance contribution) and a graduated income tax. The proponents of the schemes therefore seek to substitute for income tax and social security payments a combined system of social security payments to everyone, irrespective of taxpaying status or of need; a flat rate tax on income would then replace the existing income tax and national insurance contribution. The objectives are:

(1) To amalgamate income tax and social security into a single coherent and logical system.

(2) To remove the disincentive effects of the present income tax by substituting a flat rate tax.

(3) To simplify administration.

The Inland Revenue concludes that none of the schemes so far put forward achieves all three of these objectives, and that (1) and (2) are mutually inconsistent. A satisfactory degree of social security would need a rate of tax so high as to be disincentive. If the rate of tax is kept down on incentive grounds, the benefits will be too small to be effective as social security. And if supplementary social security payments are necessary, there is no economy in administration.

The memorandum then proceeds to consider whether the schemes have merit *either* as social security *or* on taxation grounds. In relation to social insurance, the abandonment of the contributory principle is condemned by a quotation from the Beveridge Report (Cmd. 6404, paragraph 274).

In relation to income tax, the schemes which propose relatively high rates of tax are dismissed as having a disastrous effect on incentive in the lower income

* A previous article on this subject appeared in our August issue, page 306.

groups. The *Economist* scheme and Mr. Chambers' scheme are stated merely to result in the worker queueing at one window to get his pay less 3s. or 5s. in the pound, and then at a second window to get his allowances refunded, being then left in substantially the same position as at present. In so far as the schemes alter the incidence on the individual, the same result could be achieved, if desired, within the framework of the present tax system.

Fears are also expressed that a uniform rate of tax might stimulate claims for higher wages, which could not so readily be founded on a tax varying as at present according to individual circumstances, and that the lack of detailed adjustments would lead to vigorous protests from individuals who had to pay more while others paid less.

It is suggested that the schemes as they stand would reduce the revenue by £200 million to £300 million, and that they would lose all their attraction if the rates of tax proposed were raised sufficiently to yield as much as under the present law.

The latter half of the memorandum consists of a detailed examination of the scheme proposed by the Liberal Party, leading to the conclusion that none of the claims made for it can be substantiated.

The party had decided that there was an absolute conflict between security and incentive and their scheme represented " a compromise solution."

The finances of the scheme are examined in two appendices, one showing that, owing to a series of omissions and miscalculations, there would in fact be a deficit of £315 million instead of a surplus of £265 million. The second is a table of the gain or loss to the individual taxpayer, showing that most people would be worse off, even in the lower income groups. The cash allowances of 12s. 6d. a week, of which 2s. 6d. would be offset by a reduction of food subsidies, would be too low for social security.

The claim that the scheme would restore incentives to work is answered by pointing out that, of 19 million people with earned incomes below £600 but above the exemption limit of £135, only 750,000 paid income tax at the standard rate—and only on a portion of their incomes. The remaining 18¼ million would pay at a higher rate than at present. The Board of Inland Revenue considers that a flat rate of 5s. or more on every penny of earnings must be a greater disincentive than the (1950-51) marginal effective rates of nothing, 2s. and 4s. charged only on the top slice of the earnings. " To take a homely example, it is admittedly easier to carry a weight along the level than to carry it upstairs: but nevertheless it is easier to carry a hundredweight upstairs than a ton along the level."

It is agreed that the scheme would mean a substantial saving of work to the Inland Revenue, with a probable saving in staff, after the transition period, of 10,000 to 15,000. There would also be a considerable saving in industry, and the abolition of insurance contributions would result in considerable savings to the Ministry of National Insurance. But the " personal allowances " would in effect greatly extend the present family allowances scheme. On balance, it is concluded that the scheme would mean more rather than less work in the Civil Service.

The Royal Commission's Second Session

The Royal Commission held its second series of sittings on July 17, 18 and 19, 1951, that on the middle day being in public.

After further questions to the representatives of the Liberal Party, the Commission heard representatives of the Board of Inland Revenue and the Ministry of National Insurance. The chairman pointed out that a reduction of subsidies was outside their terms of reference, and that there appeared to be several underestimates on the expenditure side of the Liberal Party's calculations.

Mr. Cockfield, for the Board of Inland Revenue, regarded the question of the national insurance contribution as irrelevant from the viewpoint of incentive; the disincentive was the impact of tax on marginal earnings. There were six million people who paid no income tax, and that could not deter them from working overtime. Under the Liberal Party's scheme a man would pay 5s. in the pound on overtime; he would get the 10s. allowance in any event, so that would not affect his mind as to overtime.

One of the advantages of P.A.Y.E. was that it swept up comparatively easily miscellaneous adjustments in a taxpayer's liability, e.g. the N.A.V. was taken into codings. This would not work under the scheme under discussion.

Some 38 million books would have to be issued, involving a net increase of staff in the Ministry of 22,000 plus 6,000 in local offices.

The chairman could not see why the " allowance " books could not be issued alongside the ration books; and if payments were made through the Post Office, he suggested that the rise in cost would not be proportionate. The Board's representatives could give no firm estimate of the cost of extra offices and accommodation.

After hearing some criticism of the estimates, they admitted that, as none of the schemes put forward went into real details, they did not quite know what they would be expected to do. Company dividends would still be taxed at source, involving repayment to those with incomes under £600. For the bulk of people below £600 a year, the proposed system was admitted to be simpler than P.A.Y.E.; the Revenue would need to issue returns to them every third year, there would be no code number, and, unless there was other income, no check at the year end. Repayments would arise for bank interest and to charities. A problem would be building society interest.

A new tax on lower income groups, restricting the existing income tax to the middle- and upper-income groups, might have advantages; it would also have disadvantages. Without knowing more about such a scheme, the witness would not like to be committed. The Liberal Party scheme might bring an additional 9 million people into taxation.

The scheme under discussion might require about 10,000 extra clerks in industry.

The next public session of the Commission is expected to be in the middle of September.

Taxation Notes

Free of Tax Annuities—Section 25, Finance Act, 1941

THE FRACTION APPLICABLE TO FREE OF tax payments under pre-war settlements, wills, etc., for 1951-52 will be twenty-one twenty-ninths. A free of tax annuity under the will of a person dying before September 3, 1939, of £200 a year, becomes £200 $\times \frac{21}{29} =$ £144 16s. 6d.

The purpose of the provision was to pass the burden of war and post-war taxation increases on to the recipient of the income, "pegging" the gross amount by reference to the standard rate in the last full pre-war year, 5s. 6d. in £, thus:

	£	s.	d.		£	s.	d.
Grossed amount:	275	17	3		275	17	3
Tax at 5s. 6d.	75	17	3	*at 9s. 6d.*	131	0	9
Net amount:	200	0	0		144	16	6

The recipient thus bears the 4s. in the £ increase.

Lack of Co-operation

Much time is wasted by the failure of Inspectors of Taxes' offices to submit computations of repayments and by their failure to show how effect has been given to set-off of tax due for repayment, e.g. against underpaid P.A.Y.E. tax.

In a recent case, the accountant wrote asking for a computation, submitting his own to show why he queried the repayment. The Inspector's office sent a computation which showed that the accountant's computation had been ignored. On the accountant pointing out two mistakes, a supplementary computation—and repayment—came to hand, but no word of apology.

It has rarely anything to do with the Inspector himself; he has to rely on his staff. But a great deal of work could be saved by co-operation. In a recent instance the Inspector wrote agreeing the amount repayable, but repaid (some weeks later) a much smaller sum. When the accountant asked the reason, he was told that the balance had been set against a Schedule E assessment in another district. Ordinary courtesy would have obviated the query here.

As this note is being written, the writer has received a hand-written memo saying:

> In reply to your letter of [14 days ago] I would advise you that the matter is receiving attention and it is anticipated that the repayment will be made at an early date.

This is a case where the figures of a Section 34 claim were agreed six weeks earlier, and tax overpaid under Schedule E (P.A.Y.E.) had already been repaid.

Another complaint is the long time accountants are kept hanging on the telephone if they try to expedite a case by ringing up to deal with a query. A little "ginger" seems needed.

Some accountants, on the other hand, fail to give the co-operation to the Revenue that is essential for smooth working. They let the side down badly, and it is not always due to ignorance! We appeal to both sides to help each other.

Maintenance Claims

It was a surprise to read in an Inspector of Taxes' letter the other day a reference to "tenant's decorations." There are no such things, except where the tenancy agreement throws some repairs on to the tenant.

The annual value is based on the rack-rent that the property would fetch if the landlord paid for repairs and the tenant paid the rates. If the agreement puts the burden of one party on to the other, the rent has to be adjusted to get at the proper annual value, just as it has to be adjusted where it is not an adequate rent.

Yet occasionally we meet the idea that a landlord is only concerned with external repairs. This is wrong; he is entitled to include in his expenditure all the repairs for which he pays.

Entertaining Expenses

Accountants will welcome the decision in *Bentleys, Stokes and Lowless* v. *Beeson* (Chancery Division, July 27, 1951), which is reported upon in our feature, Tax Cases—Advance Notes (page 351). In this case it was held that expenditure of the partners in a firm of solicitors in entertaining clients on occasions when professional advice was given and charged for in the ordinary way was admissible in computing profits. Roxburgh, J., accepted the view that the admissible expenditure included the cost of the partner's own entertainment; business would not be promoted if the partner should sit by eating and drinking nothing.

It is to be hoped that the Revenue will accept this position. It has long been anomalous that professional men, largely because they cannot advertise, have been denied relief that their clients are allowed. Particularly is this so with accountants, who have to hold the scales with equipoise and who have enough trouble with clients' expenses but are denied any relief themselves.

Double Taxation—France, Kenya, Tanganyika, Uganda and Zanzibar

The convention with France for relief of double taxation on income, which is now ratified, has been published as the Schedule to an Order in Council (S.I. No. 1388 of 1951).

Double taxation arrangements between the United Kingdom and Kenya, Tanganyika, Uganda and Zanzibar have been published as Schedules to draft Orders in Council. The arrangements require the approval of Parliament and the enactment of legislation in the territories concerned before they can come into force. They are identical in terms and follow the same general pattern as arrangements with other colonies.

Professional Notes on "Accelerated Amortisation" and International Comparison of Income Taxes appear on page 327. Letters to the Editor on page 355 discuss: Income Tax Year of Assessment; Estate Duty—Advances to Minors; Estate Duty on Timber.

Recent Tax Cases

By W. B. COWCHER, O.B.E., B.LITT., Barrister-at-Law

INCOME TAX

Income tax—Property transactions—Company with powers to deal in property and also powers to manage property—Following purchases of properties treated by Inland Revenue as investment company and management expenses claims allowed—Sales of properties at profit—Whether trading transactions—Income Tax Act, 1918, Section 33, Schedule D, Case I.

Rellim, Ltd. v. Vise (C.A., May 3, 1951), was noted in our June issue (page 223). The finding of the General Commissioners that the company was a trading company with trading profits had been upheld as a finding of fact by Wynn-Parry, J.; and a unanimous Court of Appeal affirmed their decision upon this ground. In his judgment, Lord Justice Cohen pointed out that although for six years there had been no sales that period was practically the duration of the war. The crux of the case would seem to be that the company had powers to deal in as well as to manage property, and in the words of the Lord Justice, referring to Counsel's argument for the appellant:

> Where I differ from him is that I do not think it can be said that there is any evidence which compels the General Commissioners to hold that the original acquisition of these properties was an investment.

The absence of power to deal will not preclude a Revenue claim where the facts indicate the carrying-on of a trade; but it will be of great assistance in repelling such an attack.

Income tax—Currency variations—English subsidiary company exporting petroleum products to China—Sales by means of Chinese agents—Agents required to deposit Chinese dollars with subsidiary company as security—Deposits kept in currency in Shanghai banks—Outbreak of war between China and Japan—Transfer of deposits to London and conversion to sterling—Loan of sterling equivalent to parent company—Closing down of China business—Repayment to agents of deposits—Large surplus in sterling owing to depreciation of Chinese dollar—Whether surplus a trading receipt—Income Tax Act, 1918, Schedule D, Case I.

Davies v. Shell Company of China, Ltd. (Ch. May 7, 1951, T.R. 121), was noted in our issue of February last (page 60). The facts of the case can be gleaned sufficiently from the heading. The Special Commissioners had held that as under the terms governing the deposits the company was free to use the money as part of its fixed capital and did in fact so use them and not as circulating capital the profit on exchange was a capital profit. Danckwertz, J., had upheld their decision as a finding of fact. A unanimous Court of Appeal upheld the judge's conclusion but disagreed with him in that they found that a question of law was involved. Jenkins, L.J., gave the only full judgment. He held that the deposits were loans on capital and not on revenue account and that the surplus constituted the appreciation in a capital asset not part of the circulating capital of the trade. Cohen, L.J., agreed with the view that the deposits were in the nature of loans. As the tax on £229,475 is involved and leave was given to appeal to the House of Lords, the case may go there.

In the judgment of Jenkins, L.J., two tax cases relating to exchange profits were referred to and as regards *McKinley* v. *H. T. Jenkins & Son, Ltd.* (1926, 10 T.C. 372), he said that "Both parties agree that it has no real bearing upon the present case." Nevertheless, he summarised it as follows:

> It was a case where a company in this country had to buy, for the purpose of its business, marble in Italy, and it bought lire to an amount estimated to be sufficient. . . . Lire then went up in value, and some opportunist concerned in the company's affairs seized the opportunity to sell the lire and thus make a profit. Later the company was able to re-purchase the lire at a lower price, and a profit was thus realised. Mr. Justice Rowlatt in effect held, on the facts of that case, that this was no more in effect than a bare exchange transaction in the nature of a speculation. . . .

In fact, Mr. Justice Rowlatt, for once, completely misunderstood the nature of the first purchase of lire. This, so far from being "a speculation," was a "hedge" insuring the company against the risk of currency fluctuations. It was the *sale* of the lire which was the speculation, no one being able to say what would be value of the lire at the time the currency would be needed. In his judgment in *Imperial Tobacco Co.* v. *Kelly* (1943, 25 T.C., pp. 301-2), Lord Greene, M.R., showed how Rowlatt, J., had misunderstood the position; but there is no evidence in the report of the present case that the significance of Lord Greene's examination was appreciated. As a matter of fact, the present writer would, with all due respect, suggest that the position was in an important respect essentially the same as that in the *McKinley* case. So long as the agents' deposits of Chinese dollars were covered by dollar deposits with Chinese banks, the company was in a similar position to McKinleys after the first purchase of lire. In the words of Jenkins, L.J., in the present case:

> The transaction, so long as that practice was preserved, would be a self-balancing transaction, and fluctuations in exchange would be irrelevant.

Upon the sale of the deposits for sterling, the company became, however, to use an old Stock Exchange term, an "unprotected bear." It took the risk of currency fluctuations and, without expressing any view upon the matter, it is submitted that the real question in the case is not whether the profit on the sale and repurchase of Chinese dollars was a trading transaction but whether the risk of currency fluctuations taken by the company when it sold its Chinese dollars for sterling was a trading risk giving rise to profit or loss or was a risk on capital account. The conclusion reached that the deposits were, in effect, money borrowed on capital account by the Shell organisation from the Chinese agents is remarkable.

Income tax—Cost of trading stock—Cotton spinners—Raw cotton—Payment to Cotton Controller based on company's stock position—Whether payment part of cost of cotton and to be taken into account in valuing stock-in-hand at cost—Income Tax Act, 1918, Cases I and II of Schedule D, Rule 3 (a).

Ryan v. Asia Mill, Ltd. (House of Lords, June 28, 1951, T.R. 181) was noted in our issues of September, 1949 (page 250) and February, 1950 (page 65). The case arose out of the system of bulk buying of cotton under which the Cotton Controller fixed day-to-day prices for the purchase of raw cotton and the margins to be added in ascertaining the selling prices of yarn. In August, 1942, new arrangements had been made in order to secure dispersal of cotton stocks and spinners had been urged to buy to the limits of storage capacity irrespective of their orders in hand. In the event of rises or falls in the price level of raw cotton they were to make payments to or receive payments from the Cotton Controller, according to whether their respective positions were "long" or "short" as regards the cotton required for orders in hand. The appellant company had become a participant in the scheme.

On April 17, 1944, the price of raw cotton was increased by 4½d. per pound, and as the appellant company was "long" to the extent of 2,937,993 pounds the sum of £55,087 became due and was paid to the

Controller. There was no dispute that in computing the profits for the appellant company's year ending January 13, 1945, the sum in question was a proper deduction; but, as the valuation of stock in hand at this date was to be at cost, the question was whether as regards the unsold part of the stock in respect of which the additional 4½d. per pound had been paid original cost should be increased to include this payment. The Special Commissioners had found in favour of the appellant company, holding that the addition should not be made, but Croom-Johnson, J., had reversed their decision and a unanimous Court of Appeal had upheld him. An equally unanimous House of Lords restored the decision of the Special Commissioners, reversing the decisions of the lower Courts.

The Special Commissioners had held that the £55,087 was not part of the price of the cotton which was the invoice price, the cotton being purchased out and out, but was a payment made pursuant to a commercial contract with the Cotton Controller and calculated by reference to the cover position. Their Lordships were strongly of opinion that these findings should not have been disturbed. It was a curious feature of the case that in its own accounts to January 13, 1945, the appellant company had valued the remaining "4½d. stock" on the basis contended for by the Revenue and professional evidence had been given upon behalf of the latter that this was correct from an accountancy point of view. As, however, the point was considered to be one of law, neither this fact nor the professional evidence in support counted with their Lordships. The writer in his previous notes expressed the view that the point was a fine one, and the division of judicial opinion is noteworthy. It remains to be seen how far the principles established will be sought to be applied.

ESTATE DUTY

Estate duty—Legacies—Provision in will whereby death duties at the rates in force at the date of will to be paid and discharged out of residue—Whether legacies free of foreign death duties—Estate duty on settled pecuniary legacy—Double estate duty agreement — Apportionment of relief — Double Taxation Relief (Estate Duty) (Canada) Order, 1946, No. 1884.

In re Cunliffe-Owen (Ch., April 12 and June 6, 1951, T.R. 155) arose out of the will of testator who died possessed of large interests in many parts of the world. He left, *inter alia,* certain legacies and directed that the death duties payable in respect thereof at the rates in force at the date of his will should be paid out of residue. One of the questions which arose was whether this direction was to be construed as referring only to U.K. death duties. Wynn-Parry, J., after considering *In re Norbury* (1939, Ch. 528), *In re Quirk* (1941, Ch. 46), and *In re Frazer* (1941, Ch. 326), held that the rule whereby *prima facie* such a direction referred only to U.K. death duties was not displaced by the facts of the case and that the limitation applied. A second question arose out of the special conditions attaching to one of the legacies; whilst a third question, one of general interest, arose out of the Double Taxation Relief (Estate Duty) (Canada) Order, 1946 (No. 1884), and a Revenue concession regarding South African succession duty in respect of which there was no double taxation agreement. In the case of both countries it had been shown that the duty was a charge on the "successor." The judge held, in effect, that the credits for foreign duty were to be distributed not according to the personal taxation liabilities to such duty but according to the legatee's respective interests in the assets available for the payment of the legacies, e.g. as regards the residuary legatees in proportion to their respective interests in the residuary estate.

The decision upon the last point will probably be of value to executors: but it covers new ground and in view of the many double taxation agreements either concluded or pending, further judicial exploration of the problem may be expected.

Estate Duty—Cesser of interest—Settlement—Trustees to keep up assurance policies on life of father—Father no interest in policies on his own life, having sold the same for full surrender value to trustees—Death of father—Policy moneys paid to trustees—Life interest in trust income continuing. Whether a cesser of interest on death of father due to cessation of assurance premiums—Finance Act, 1894, Sections 2 (1) (b), 7 (7).

In re Brassey's Resettlement (C.A., June 20, 1951, T.R. 173) was noted in our issue of March last (page 113). The premiums upon the policies in question payable by the trustees of the settlement amounted to £1,977 per annum and on the death of Captain Brassey, the father, produced £40,000. The issue was whether upon his death there was, within Section 7 (7) of Finance Act, 1894, the "cesser of an interest" giving rise to benefit. Romer, J., had held that in the event of the trustees not keeping up the policies the remaindermen entitled to the reversion under the settlement could have compelled them to do so. This power, he held, constituted an "interest" which of necessity ceased when the policies matured on the death of the assured and this cesser gave rise to benefits in various ways affecting the deceased's widow, the tenant-for-life, and the remaindermen. Having come to this conclusion, the "slice theory" based on Section 7 (7) applied. A unanimous Court of Appeal affirmed this decision, the Master of the Rolls giving the only full judgment, one which showed what harsh "non-sense" the "slice theory" can give rise to. One of several striking passages was:

> The claim under Section 2 (1) (b) is not, however, a claim to exact duty upon that sum (£40,000). As Mr. Pennycuick for the Commissioners of Inland Revenue explained, the benefit that arose by receiving the policy moneys is, for present purposes, an irrelevant benefit. There is perhaps a certain irony in that concession, for Mr. Pennycuick and Mr. Stamp have made it clear that the somewhat obscure provisions of the Finance Act, 1894, are apt to work in a rather mysterious way.

He then referred to the fact that during the period between 1935 and 1946, £1,977 per annum was diverted from the life tenant for payment of premiums and that:

> Upon the death of Captain Brassey that diversion ceased and £40,000 was received. But if the Crown's claim is right, as I have felt constrained to conclude that it is, *the duty exigible,* which arises out of the provisions relating to the policies, appears to amount to a sum of £60,000 to £70,000, not less than 50 per cent. more than the capital value of the policies, a result which, by depriving Hugo (the tenant-for-life) of £1,977 per annum, the trustees in the due performance of their obligations have managed to achieve.

He then went on to suggest that if the trustees had had prophetic vision they would have done better to have burnt the policies on the day following the re-settlement and thereafter refused to pay the premiums although, for the Crown, it was pointed out that had they done this they would have been even worse off unless Captain Brassey had survived the bonfire by the statutory period of (then) three years.

Whilst the "benefit" from the policies was £40,000, the "slice" of the estate which £1,977 income represented came to "a figure of £104,000 or £105,000." Leave was given to appeal to the House of Lords, and, if availed of, it will be interesting to see what that Court has to say upon the subject.

Estate duty—Bequest of 25 annuities—Direction to appropriate out of estate annuity fund—Estate insufficient for purpose—Testatrix's children residuary legatees—Purchase of annuities from children—Agreements that purchased annuities to be sole security for payment of will annuities—Death of an annuitant—Whether cesser of interest whereby benefit accrued or arose—Whether interest ceasing on death disposed of or determined—Finance Act, 1894, Sections 2 (1) (b), 7 (7)—Finance Act, 1940, Section 43.

In re Beit (Ch., June 6, 1951, T.R. 133) arose out of the will of Dame Lilian Beit,

who died on November 7, 1946. Testatrix bequeathed some 25 life annuities and the executors were directed to appropriate an annuity fund sufficient to produce at the time of appropriation income to provide the annuities after deduction from the said income of tax at the standard rate. One annuitant, a Mrs. Carter, was bequeathed an annuity of such an amount as after deduction of income tax at the standard rate would leave her £52 12s. There were other bequests out of the balance of the estate. The residuary legatees under the will were testatrix's three children. Mrs. Carter had died on November 18, 1947; and the questions before the Court were whether Estate Duty was payable and, if so, how the amount was to be ascertained and to what extent the executors were liable. What would have been a comparatively simple problem had, however, become complicated by events subsequent to testatrix's death.

The estate was found to be insufficient to constitute an annuity fund with an income large enough to pay the annuities, and the executors, who under the will were empowered to purchase annuities from the Government or an assurance company, resolved to provide them by purchasing corresponding annuities from the three children. These were to be charged and secured not on the general estate of the testatrix nor on any annuity fund, but solely on a joint and several covenant by the children to pay to the executors annuities of similar amounts to those payable under the will. All of the annuitants, save one who did not reply and another who disclaimed, agreed to this arrangement and the executors paid to the children £60,904 18s. 4d., being the actuarial value of the annuities other than the one disclaimed. The effect of this arrangement was that the executors paid the will annuities out of the substituted annuities. On the death of Mrs. Carter, the Revenue claimed that Estate Duty was payable in respect of the cesser of her annuity either under Section 2 (1) (*b*) of the Finance Act, 1894, or under Section 43 of the Finance Act, 1940. The former operates where any benefit arises or accrues from the cesser of an annuity, but so far as the estate was concerned the benefit of cessation of the will annuity was balanced by the cessation of the children's annuity, whilst the children themselves were in the same position as an insurance company. As regards the second ground, Section 43 imposes duty where an interest limited to cease on a death has been disposed of or has been determined, and for the executors and trustees it was contended that the interest here was the will annuity which was never paid, whilst for the Crown it was argued that it was the right to receive the will annuity out of the estate and that this was disposed of or determined by the arrangement and, alternatively, that the will annuity was itself determined at the time of the arrangement.

Vaisey, J., considered that the "situation is irresolvably ambiguous in character"; but held that the plaintiff's contention was "preferable or at least equally tenable" and decided that the Revenue claim failed. As this case opens up certain possibilities, it may go further.

Tax Cases—Advance Notes

By H. MAJOR ALLEN, Barrister-at-Law

House of Lords

Birmingham Small Arms Co., Ltd. v. C.I.R. June 20, 1951.

The facts in this case and the Court of Appeal judgment were reported in Accountancy for September, 1950, page 326.

The House of Lords dismissed the company's appeal.

Divisional Court (Goddard, L.C.J., Hilbery and Ormerod, JJ.)

R. v. Gen. Commissioners for Morleston and Litchurch (*Ex parte* G. R. Turner, Ltd.). July 27, 1951.

Facts.—This was an application for an order of prohibition directed to the Commissioners (*a*) to restrain them from proceeding to re-hear an appeal, and (*b*) to prohibit them from stating a Case in the form of the draft prepared by them.

After hearing argument on behalf of the appellants (G. R. Turner, Ltd.) and of the Inspector at the hearing of an income tax appeal, the Commissioners directed the parties to withdraw while they considered their decision. After a lapse of time, the parties were recalled, and the Clerk, in the presence of the Commissioners, read out what purported to be their decision in favour of the taxpayer. The Inspector thereupon expressed dissatisfaction, and in due course required a Case to be stated. The Commissioners prepared a draft Case which set out the facts and contentions of the parties and stated that the Clerk had erroneously read the Commissioners' decision as being in favour of the taxpayer, when in fact it was in favour of the Revenue.

Decision.—Held, that the Commissioners, not having amended the assessment, had not formally determined the appeal and were at liberty to alter their decision or to correct an incorrect statement of that decision. In view of certain irregularities of procedure, however, the Commissioners were ordered to pay their own costs.

Chancery Division (Roxburgh, J.)

Wildbore v. Luker. July 25, 1951.

Facts.—The appellant was tenant and licensee of a public house, which consisted of two rooms used as bars, and four rooms used by him as residential accommodation. It was agreed that two-thirds of the rent paid was properly deducted in arriving at the trading profits. The taxpayer, however, contended that the proper deduction in respect of rates should be arrived at as a result of an apportionment made between the bars and the private accommodation. The Inspector, on the other hand, declined to admit a deduction exceeding two-thirds of the total rates paid.

The General Commissioners decided in favour of the Inspector.

Decision.—Roxburgh, J., held that Rule 3 (*c*) of the Rules of Cases I and II of Schedule D was not applicable, and remitted the case to the Commissioners to reconsider a proper apportionment of the rates.

Bentley, Stokes and Lowless v. Beeson. July 26 and 27, 1951.

Facts.—The appellants, a firm of solicitors, claimed as deductible in computing their profits certain "entertainment" expenses, consisting for the most part of the cost of lunches with clients, at which professional business was discussed.

The Special Commissioners, while accepting that the expenditure was incurred for business purposes, held that it was not necessary for those purposes and disallowed the deduction.

Decision.—Roxburgh, J., held that the Commissioners had applied the wrong test. Since the expenditure was "wholly and exclusively" incurred for business purposes, the taxpayers were entitled to the deduction claimed.

(This case is referred to in a Taxation Note on page 348 of this issue.—Editor, Accountancy.)

The Student's Tax Columns

LOSSES—I

Let it be emphasised at the outset that there is no such thing as a " minus " assessment. While assessment of business profits is on the preceding year basis, if there is no profit, the assessment is " nil."

It is therefore important that there should be express provision for relief for losses; a business man ought not to pay tax in good years without relief for bad years. But there can be no relief unless the Acts provide specifically for it. In this article, an introduction is given to the reliefs without going into " tricky " applications of them, or into concessions.

Section 34, Income Tax Act, 1918

The first relief is under Section 34, whereby, if a loss is suffered in a trade, business, or profession, the taxpayer may claim to set the loss against his total income of the same year, and obtain relief from tax payable accordingly.

Strictly, the loss ought to be that of the income tax year ending April 5, but there is no objection (except in the opening and closing years of a business, or in a year following a claim on the " income tax year " basis) to taking the loss of the accounting year ended in the income tax year.

The repayment (relief) from tax cannot exceed the tax suffered, or tax on the loss. As the loss is a loss of earned income, it is set first against earned income.

Illustration (1). Individual, 1950-51 (ignoring family allowances and National Insurance contributions).

		£	s.	d.
Business assessment (profit of year to 31.1.50)		2,600		
Wife's earned income		600		
House N.A.V.		50		
Dividends		1,000		
		£4,250		
Less Ground Rent and Mortgage Interest	£320			
Bank Interest	30			
		350		
Statutory Total Income		£3,900		
E.I.R.	£400			
P.A.	180			
Additional (wife)	110			
Two children	120			
Life Assurance, 2/5 × £600 ..	240			
		1,050		
		£2,850		
£100 at 2s. 6d.		12	10	0
400 at 5s.		100	0	0
2,350 at 9s.		1,057	10	0
£2,850 Tax borne ..		£1,170	0	0

In the year to January 31, 1951, a loss of £3,000 was made. This must be set first against the husband's earned income, then against his unearned income; the wife's income cannot be touched in respect of the husband's loss until his income is exhausted.

The revised computation becomes:

Wife's earned income		600
Husband's unearned income (balance) ..		650
		£1,250
Less Annual Payments, etc.		350
Revised Statutory Total Income		900
E.I.A. (wife only)	£120	
P.A.	180	
Additional	110	
Children	120	
Life assurance (N.B.) 2/5 × 1/6 × £900	60	
		590
		£310

Note.

	Husband		Wife
	£		£
Statutory Income ..	300		600
E.I.A.		£120	
Additional Personal ..		110	
Other Allowances ..	300	60	
			290
			£310

	£	s.	d.
£50 at 2s. 6d.	6	5	0
200 at 5s.	50	0	0
60 at 9s.	27	0	0
Amended tax to be borne	83	5	0
Original tax to be borne	1,170	0	0
Tax repayable ..	£1,086	15	0

Proof:

Loss		£3,000		
Allowances no longer available:				
E.I.A., £400 — £120 =	£280			
Life assurance, £240 — £60 =	180			
		460		
Tax at 9s. on		£2,540 =	£1,143	0 0
But there has been lost the husband's reduced rate relief:				
£50 at 6s. 6d. (being 9s. less 2s. 6d.)	16 5 0			
and £200 at 4s. (being 9s. less 5s.)	40 0 0			
			56	5 0
Reclaimable			£1,086	15 0

Illustration (2). Company's results:
Year ended December 31, 1949 Profit, £1,200
Year ended December 31, 1950 Loss, £900

Ignoring capital allowances, the company will be assessed for 1950-51 on £1,200, tax on which at 9s. = £540. A Section 34 claim would give relief of £900 at 9s. = £405, leaving the company to bear tax on £300 at 9s. = £135.

Illustration (3). Had the above company paid debenture interest of £400 in 1950-51, the position would be as follows:

Assessment 1950-51 ..	£1,200
Less Debenture Interest	400
Statutory Total Income	£800

As the company recouped tax on £400 from the debenture holders, it can recoup tax on only £800 under Section 34, suffering no tax. This leaves £100 loss to be carried forward under Section 33, Finance Act, 1926, or for relief under Rule 13, dealt with below.

The effects are often numerous. In Illustration 1, the total income is reduced to such an amount that the one-sixth limit operates on life assurance premiums; and the husband's income is wiped out and his reduced rate " lost." Sometimes other allowances are " lost." But a Section 34 claim does put money in the " kitty " in the year the loss is incurred.

(*To be continued*)

FINANCE

The Month in the City

Attack on Equities

THE EVENT OF THE MONTH HAS BEEN MR. Gaitskell's proposals to deal with the economic position—in particular, his plans to stabilise dividends which have not been raised and to reduce those which have. The scheme would have been received badly enough in the City even if it had been part of a really genuine scheme for preserving the value of money, but as it is felt that less than nothing is being done to that end, there is some excuse for regarding the new proposals as predominantly a political gesture. Their effects are made even worse by the absence of any firm interpretation of the White Paper, which purports to explain the Government's intentions, until the legislation is in force, perhaps many months ahead. Something definitely unpleasant had been expected, but nothing quite so far-reaching as this. The effects in the Stock Exchange were " good fun " to Mr. Dalton, and his curious ideas of what constitutes fun extracted a reply from Mr. John Braithwaite, chairman of the London Exchange. Formally a reply to the former Chancellor, the letter also exposes the effects of the policy of his successor upon investors in general and upon the whole business of financing the country.

New Issue Uncertainties

One of the more obvious problems presented by the White Paper confronts those wishing to make new issues, particularly of Ordinary shares. The position of a company which offers further shares of a type already dealt in may be reasonably clear. But there is no possibility of saying what will be the position of a private company which, either because of estate duty or because it needs more money than can be provided by the existing shareholders, is being sold to the public. Perhaps new money can be obtained through bank advances, if the activity carried on is one of which the authorities approve. But, in the absence of any firm control over the total amount of credit created, operations of this kind will certainly not dampen down the inflation. The market seems to suppose that for some months at least there will be few, if any, offers of Ordinary shares. There is more than a possibility that the practice of raising capital by short term bond issues will become even more popular. Reflections like this are one of several factors tending to prevent anything like a flight from equities.

Speaking Out

To return to Mr. Braithwaite's letter, before he sent it there was a good deal of difference of opinion in financial circles whether or not this was an occasion for comment. Since it was published, more and more people would like to see a general statement of views by representatives of the leading bodies connected with finance in its many aspects. So long as it was possible to claim that everybody was making sacrifices, it could be argued that dividends could bear a heavier cut than some other forms of income, although it is very doubtful whether the argument was a reasonable one so far as concerns the majority of holders of Ordinary shares. Now, however, not only are equity holders to bear what looks like a quite disproportionate share of the burden, but the means adopted threaten him with the permanent loss of the returns of risk-taking and abstinence. In the interests of the country at large, no less than of the individuals directly affected in their pockets, the growing opinion in the City is that the time for very plain speaking has come. It may not affect the final outcome, but that is no reason for letting the case of the financial world go by default.

The Modest Decline

To put the market reaction to Mr. Gaitskell's statement in perspective, it is necessary to go back a little. The recent peak of the index of industrial Ordinary shares, compiled by the *Financial Times*, was 140.4 on June 14. On the eve of the announcement there had been a fall of 7.5 points and, in the ensuing three business days, this was carried a further 5.8 points. But the next few days brought a recovery of 3.7 points, a net fall of 1.58 per cent. since July 26 and of 6.83 per cent. since the recent peak. Meanwhile, the rise in the average yield on Ordinary shares is from 4.80 per cent. on the eve of the announcement to 4.91 per cent., while that on Old Consols has remained unchanged at 3.80 per cent. The Ordinary share yield appears to be calculated on the latest dividends, however, not on those to be expected and, if this is so, the yield demanded has probably risen little, if anything, since the announcement, although it has increased by one-tenth since June 14. This seems to suggest extreme optimism on the part of the investor. Either he believes that there will be a change of Government, or he is more convinced than ever that there will be inflation and that equities, even with their present disabilities, do afford some protection. However, he may be rather less logical than this would suggest. It may merely be that, having held off for the flow of new offers which he expected, he now realises that these are likely to be held up indefinitely,

and thinks that even a small fixed return is better than money in the bank.

Since the middle of the month, markets have been rather inactive with a sagging tendency. The main changes on the month are reflected in the following changes in indices of the *Financial Times* between July 24 and August 21 : Government securities from 101.78 to 101.95, the yield on Old Consols from 3.80 per cent. to 3.78 per cent., industrial Ordinary shares from 132.7 to 132.8, gold mines from 109.65 to 112.44.

Points from Published Accounts

Footnote Items

IT IS BECOMING INCREASINGLY POPULAR TO strike the prime profit brought to profit and loss account after making several deductions. These are contained in a panel and sometimes an aggregation is not made. Another method is to relegate items to a footnote. *Carpet Trades,* for example, shows the trading profit in the consolidated accounts subject only to directors' fees and taxation. Relegated to a footnote are depreciation; contributions paid under the staff pensions scheme and the superannuation endowment trust; an additional amount set aside for pensions; management directors' remuneration; the audit fee; and expenses. In the aggregate these items are greater than in the preceding year, but the accounts still show that the trading profit has soared—to such an extent that the relegation of these items to an inconspicuous position at the foot of the accounts is not solely a diplomatic move. Incidentally, the profit and loss account is not encumbered by a mass of items, and their excellent lay-out would not have been impaired by the inclusion in the body of the account of the items stated.

Comparative Figures, 1936-51

On the back page of its report and accounts *Revo Electric* includes comparative figures for 1936-51, showing the issued capital, reserves, the total of capital and reserves, fixed assets, net current assets, and the percentage of net dividend on the capital employed at the end of the accounting period. The first year shows total capital and reserves of £369,794, and the net dividend on capital employed at 10.92 per cent. Since 1947 the last column shows a continuous reduction in the net dividend rate on capital employed from 5.70 per cent. to 3.95 per cent., although the total of capital and reserves has grown since 1936 to £1,356,501. This is the result of the dividend freeze, and considerable profits retentions.

For reasons which are not self-evident, the balance from trading account is shown after making provision for directors' fees, depreciation, staff pensions, and one other item. A footnote to the balance sheet indicates that "provisions for taxation do not include additional profits tax which would be payable in the event of a subsequent distribution of retained profits, and which would amount to approximately £166,000 (1950, £121,500) before providing for such income tax relief, as may be obtainable thereon." The writer shocked a company director recently when he pointed out that a significant part of the reserve appropriations that had been made since the birth of distributed profits tax was illusory. Not all companies go to the trouble of indicating the extent to which this is so.

Another company to show various items in a panel, and a profit for the year after deducting them, is *Vitamins.* It is not alone in recognising the abnormally low tax provision—in this instance deriving from initial allowances, research expenditure and other matters—by a reserve transfer. The amount transferred is £35,000, but whether or not this is a full acknowledgment of the taxation relief is not stated. However, the dividend, grossed-up, is in very small relation to the profits before tax. It may be contended that shareholders should not have to go to the trouble of making a calculation of this kind in order to place the cover for their dividend in perspective.

The Pye Report

The report of the directors of *Pye* consists almost entirely of footnotes to the accounts. These notes appear at the end of the tabular profit and loss account, and for legal purposes this method is evidently adequate. At any rate, it clears the way for presenting a novel "annual report" which we shall comment upon later in this note. Before striking a "total available for distribution" — this includes the balance brought forward from the previous year—there are seven items of what may be termed an accidental nature. (Some people have an objection to the alternative phrase "exceptional nature," so the alternative has been used. A better phrase even than these two might have been "coincidental nature," to stress that the results of the year have been affected by events that might never have taken place.) For instance, there are (*a*) losses, less profits, on disposals of fixed assets, (*b*) losses on exchange, (*c*) expenses of share issue, and (*d*) formation expenses of subsidiaries. Agreed, these sums are not "available for distribution," but should they be deducted before striking the total under this head? Or should their "accidental" (or "exceptional" or "coincidental") nature have been acknowledged by deducting them after charging the dividends, so that shareholders can see the notional normal cover for their payments? Again, is it of value to shareholders to deduct transfers to staff pension fund and to general reserves for bad debts, before striking that ambiguous "total available for distribution"? This balance is not all available for distribution *to shareholders,* because there is an employees' profit-sharing scheme which had been in direct relation to dividend payments. It is necessary to use the past tense, but even if it had not there is an added complication that the employees are entitled to their "whack" along with the equity shareholders.

The method of rewarding employees *pro rata* to the Deferred Ordinary stock dividend had a flaw in it. Last August it was announced that the directors would review the situation to take care of a difficulty which arose because the big increase in the number of employees would have meant a fall in their individual bonus entitlement. There are pitfalls in profit-sharing schemes! It must have been a difficult task to decide on the best way of presenting the accounts, but we have the feeling that the form could have been improved upon.

The "annual report" is an excellent affair consisting of a series of articles that should be of interest to all shareholders. These are, we presume, a distillation of the views of the board on rearmament, on dealing with Government departments, on the Beveridge Committee report on broadcasting, and on the B.B.C. monopoly. There are amusing cartoons, and the one of Sherlock Holmes and bloodhound, don, chemist and others examining a weird and wonderful balance sheet is a real gem. The report is, in fact, intended as an answer to an article in the *Financial Times* which suggested that, on the evidence of an investigation in the U.S.A., if shareholders could have, in a few easily understandable

words, the story of their company during the previous twelve months, it would be of far greater interest to them than a mass of figures. The third paragraph states:

> After providing for the full dividend on the Preferred Ordinary stock we made over 6s. profit per 5s. Deferred Ordinary stock unit. The figure for the previous year was 9s. but as the Deferred capital was doubled by a free bonus of 100 per cent. issued during the year, the real comparative figure for last year is 4s. 6d.

But in reviewing the annual report the *Investors' Chronicle* said that this statement "must, if it means anything at all, mean that earnings were 120 per cent. We prefer our orthodox method of calculating earnings which eliminates, as far as we are able, the extraneous profits of the year and works back from the net profit and allows for the full weight of profits tax that would be attracted on entire distribution. We calculate earnings at only 48¾ per cent., though we take profits for this purpose after the deduction of £32,000 for the workers' bonus, whereas the Pye management may argue that this is not compulsory."

Fixed Assets Replacement—"Re-equipment" and "Equipment" Reserves

The report of *Renold and Coventry Chain* points out that previous references have been made to the problem of providing for the replacement at current prices of equipment acquired when costs were much lower, and that continued inflation during the year has aggravated the situation. An investigation has been concluded, and in the light of its findings the directors have adopted the view that, at the date of any balance sheet, the cumulative depreciation plus the re-equipment reserve should represent what the cumulative depreciation would have been if the equipment existing at that date had been acquired at the prices ruling during the year. That is to say, the re-equipment reserve should represent additional cumulative depreciation so that, as far as can be estimated, the aggregate amount of reserve and direct depreciation accumulated during the life of an asset will be sufficient to buy a new asset at the price current when the old one becomes worn out or obsolete. Accordingly, when an asset is replaced not only is the amount it has contributed to cumulative depreciation taken out of that account and used to write off the original cost of the asset replaced, but also the amount which it has contributed to re-equipment reserve should be taken out of that reserve and credited to a new reserve—to be called equipment reserve—which latter would then represent the retained profit which has actually been spent in replacing assets at an enhanced cost.

The investigation also revealed the extent to which fully depreciated plant and machinery were still in active and efficient operation. The history of various classes of equipment was examined, and the directors considered that rates of depreciation at a lower level than hitherto would more accurately reflect current experience. They therefore decided that new rates of depreciation should be adopted, and that the cumulative depreciation at the beginning of the current financial period should be reduced to the amount which it would have been had the new rates of depreciation been applied throughout the life of assets existing at the year-end. The re-equipment reserve has, then, been built up by a transfer from general reserve and the balance of depreciation adjustments.

Letters to the Editor

Income Tax Year of Assessment

SIR,—Replying to your correspondent, T. E. Brown (ACCOUNTANCY, August, 1951, page 308), I would suggest that the apparent difference of one day arising in his explanation of the change in the end of the Government's financial year to April 5, is due to an error on his part.

He states that eleven days were omitted after September 2, 1752, making the next day September 14; but in his next paragraph he adds eleven days to March 24 to give April 4, or an apparent difference of one day in the end of the financial year as it now is. If, instead of this, he added eleven clear days to March 24 (i.e. March 25 to April 4) the next day becomes April 5, and there is no difference calling for explanation.

Yours faithfully,

Newton Abbot, GERALD J. KING.
August 9, 1951.

Estate Duty—Advances to Minors

SIR,—In your copy of ACCOUNTANCY for July, 1951, on page 271, you deal with estate duty on advances to minors. In the case of a beneficiary succeeding absolutely by reason of the exercise of a power of appointment by will it is stated that the trustees are considered to be accountable for any duty that may be payable in respect of advances made to him on account of his presumptive share. In view of the fact that the amount advanced may be considerably in excess of the appointed sum, it is not stated out of what fund the duty would be found. It is presumed such duty would be charged against the general fund before carrying into effect the appointments made but perhaps you will let me know whether you are in a position to advise on this point, as the incidence of the duty is one of the utmost importance to the trustees. It will also, of course, be necessary to bear this in mind when deciding whether or not to make an advance in respect of a presumptive share.

Yours faithfully,
SIDNEY H. BARR, A.S.A.A.

London, E.C.3.
August 14, 1951.

[We are advised by the Board of Inland Revenue that in their view the duty as assessed must be paid out of the funds remaining in the hands of the trustees. The balance remaining after satisfaction of the duty and costs is then divisible amongst the beneficiaries according to their respective interests, each beneficiary bearing a share of the duty proportionate to his benefit. For this purpose advances liable to duty count as benefits, but advances not liable to duty are ignored.—Editor, ACCOUNTANCY.]

Estate Duty on Timber

SIR,—I should like to thank you very much for reviewing so favourably my book, *Agricultural Death Duties*, in your August issue (page 313), but may I correct a misunderstanding on the part of your reviewer? He refers to a flaw in my reference to the rate of interest on estate duty on timber (which I gave as 3 per cent.), and says that the correct charge is 2 per cent.

Although it is true that by virtue of Section 27 of the Finance Act, 1943, the usual rate of simple interest payable in respect of outstanding estate duty is 2 per cent., the rate of interest on duty on *timber* is fixed at 3 per cent. by Section 9 of the Finance Act, 1912.

I was particularly careful to check this apparent anomaly with the Estate Duty Office before passing the book for publication.

Yours faithfully,

London, W. WALKER WATSON.
August 9, 1951.

[Our reviewer apologises to Mr. Watson, whom he thanks for an addition to his knowledge.—Editor, ACCOUNTANCY.]

Publications

AUDITING PRACTICE. By R. R. Coomber. (*Macdonald & Evans, Ltd., London. Price 21s. net.*)

Written both for students preparing for examinations and also for those who are already in practice, *Auditing Practice* has been designed, in the author's own words, "to give a general statement of the practical side of auditing procedure." At the same time an exhaustive consideration of all the many-sided problems which may arise in the daily practice of an accountant has not been attempted, nor have rigid standards of procedure which should be adhered to in all cases been suggested. Nevertheless, in attaining his object the author has in no way failed to do justice to his subject, which, as will be seen from the Table of Contents (in itself a second index), has been presented in a straightforward and logical sequence.

Auditing methods, the audit of subsidiary books and records, and of ledgers, are dealt with in successive chapters, before the verification of assets and liabilities. In each of these chapters, the audit procedure indicated follows on strictly practical lines, with particular stress on the system of internal check in force and the extent to which the auditor may rely upon it.

A chapter has been devoted wholly to provisions for depreciation, reserves and sinking funds, and although it might be considered that much of its content is outside the scope of a work on audit procedure, it cannot be denied that the method adopted enables the reader to obtain a clear understanding of this topic and its bearing upon the work of the auditor.

Having dealt with basic procedure common to all audits, whether the accounting records be compiled manually or mechanically, attention is turned to particular audit problems of the various forms of proprietorship, followed by a detailed consideration of the audit of the accounts of limited companies, with a separate chapter on matters of audit routine in relation to companies. Here again, the author has not concerned himself merely with audit procedure, but has contrived within the space of little more than seventy pages to bring to the reader's notice those provisions of company law which bear particularly on an audit, and to deal with the Eighth Schedule to the Companies Act, 1948, which has been incorporated, with the Companies (Shipping Companies Exemption) Order, 1948, and Extracts from Table A, as an appendix.

Holding and subsidiary companies, group accounts and their audit have been treated in the same way, and it is pleasing to note that an example of consolidation statements and accounts has been included to show in simple form the method of their preparation and the summaries which would be prepared and presented to the auditor.

The outstanding feature of the chapters on profits and dividends and on the auditor's liability is the treatment of those decided cases forming the foundation of this part of the subject, which, with extracts from the more important passages in the judgments, have been presented in an interesting and informative manner.

The remainder of the book is devoted to practical aspects of investigations and consideration of audit reports and certificates, again including examples of published accounts and reports.

It will not detract from the signal merits of this book if two minor slips in the text are noted. Firstly, in the last paragraph on page 202, the reference given should be to Part I, para. 11 (4) of the Eighth Schedule, and secondly, in dealing on page 337 with the provisions of Section 55 of the Finance Act, 1940, the period during which control must have been exercised by the deceased should be five years before death, in view of the amendment by Section 47 of the Finance Act, 1946. G. W.

FINANCIAL CONTROL: ITS PLACE IN MANAGEMENT. By five contributors. (*Published for the Institute of Public Administration by Macdonald and Evans, Ltd., London. Price 6s. 6d. net.*)

The purpose of this book is to give a comparative survey of financial control in a Government Department, a local authority, a public corporation and an industrial undertaking, and in small compass it does an excellent job. The authors of the four main chapters speak with authority and illustrate very clearly how differences in type of financial operation, tradition and environment affect both the nature of financial controls and the approach to them. Briefly, there are two main concepts of financial control—a control of financial transactions and the utilisation of financial data for managerial control. Both are inherent in any effective system, but the weight given to each of them and the extent to which each forms part of the final system vary widely.

Mr. Barnes, of the Ministry of Fuel and Power, describes a system which, in spite of special and interesting devices to deal with trading activities, is largely governed by the needs to obtain parliamentary sanction for expenditure and to see that the votes are not over-spent. The emphasis here is more on amounts of money than on moneys' worth. Dr. Marshall's provocative chapter on local authority finance shows, in some respects, a similar approach, but he demonstrates, too, that in the local authorities (as distinct from the Government Department) there is both a greater flexibility in financial administration and a greater recognition—though apparently it is not yet universally accepted by elected representatives—of the need to budget in advance and to control and watch the expenditure while it is actually being incurred. Mr. Haworth's chapter on a Port Authority deals with an interesting and rather individual case where, for special reasons, precise budgeting is not possible, and money-consciousness on the part of officials is maintained by a detailed system of financial reporting. Mr. Ryan's chapter on the industrial concern presents yet another picture. Here we are in a competitive world, there are shareholders to be satisfied at the end of the day, and financial data play an important part in determining policy and controlling operations. Forecasts and budgets are basic to the system, but the main implement of day-to-day control is a series of periodical progress reports which permit the state and prospects of the business to be kept under constant review and permit effective action while things are actually happening.

In a summing-up chapter, Mr. Oscar Hobson differentiates the static from the dynamic financial controls—it is hardly necessary to say which is which.

There are some passages in the various chapters which not all readers would readily accept without argument, but there emerges from the book a clear and encouraging picture of an attempt, over a very wide field, to make figures something more than mere records. Obviously, varying conditions prevent the adoption of the same methods everywhere, even in apparently similar undertakings, but the principles of consideration before action, examination of control papers, while the work is going on and study of the results for future guidance, are universally applicable. There is still scope for a greater appreciation of what can be done in this way, and Mr. Ryan's paper in particular may provide, for commercial concerns, a basis for working out an effective system of financial control of their own. Perhaps Mr. Ryan makes it seem too easy—but that is hardly a fault when selling an idea. P. G. J.

Legal Notes

Notice to redeem mortgage—Right to interest subsequent to expiry of the notice.

There is a line of cases to the effect that, even if there has been a tender by a mortgagor of the amount due for principal and interest, that tender does not stop interest running after the date of the tender unless there is evidence that the sum has been set aside and is ready for payment at any time. There are also other cases tending to support the proposition that, when the delay in redemption is caused by the wrongful conduct of the mortgagee, interest does not continue to run.

In **Barratt v. Gough Thomas** (1951, 2 A.E.R. 48), Danckwerts, J., applied the first principle on the facts before him. B. had given notice that he proposed to redeem a mortgage on a date in 1943. The mortgagees then set up a claim to a lien on the deeds for some costs incurred by B. and refused to hand over the deeds unless B. paid the costs as well as the moneys due under the mortgage. There was protracted litigation, in which it was finally held that the mortgagees had no lien, and the mortgage was not paid off for some years. The learned judge found that there was no actual tender and that the money had never been set aside for repayment. The mortgagor had therefore had the use of the money between 1943 and the date of repayment. Although the delay was due to the mistaken claim of the mortgagees, it was right that the mortgagor should pay interest over this period.

Construction of wills.

B., a director of a company, bequeathed "to each member of the staff of the company who shall have at my death had not less than five years' service with the company a sum representing three months' salary and emoluments at the rate payable to him or her at the date of my death."

In **re Bedford, decd.** (1951, W.N. 310), Danckwerts, J., was asked to construe these words and his lordship held as follows:

(*a*) in the circumstances of the case, "staff," a word of many different meanings, described a smaller class than would have been described by such a word as "employees": it meant those persons not paid by piecework rates, but remunerated on a salary basis by reference to the week, month, quarter or year, and not paid overtime;

(*b*) there was no need for the five years' service to have been continuous: separate periods of service could be aggregated;

(*c*) war service did not count as service with the company, even though the directors had resolved in 1940 that an allowance should be paid to employees who, with the company's consent, joined the Forces.

Powers of gas officials to enter premises.

The case of the gas inspector who entered a house during the absence of the occupier was given considerable publicity in the newspapers and has now been reported in **Grove v. Eastern Gas Board** (1951, W.N. 312). Collectors of the Gas Board had from time to time entered the house with the knowledge of the occupier as a matter of routine, reading the meter, collecting the money from it and inspecting the fittings. There came a time when the collector could not get a reply from anyone in the house. Three further abortive calls were made, and finally an inspector, taking with him a carpenter and an authority to enter, called at the house and received no reply. He then had the front door opened and went in. After collecting the money from the meter and inspecting the fittings he went out again leaving the door as securely fastened as it was originally.

The occupier sued the Gas Board in trespass, but Hilbery, J., held that the Board was entitled to enter in this way. The argument before the Court largely turned on the construction of paragraph 34 of the Third Schedule to the Gas Act, 1948, and the learned Judge said that, broadly speaking, the intention was to give Gas Boards the same powers as those possessed by the former undertakers: under earlier legislation those undertakers would have been empowered to enter in the circumstances of this case.

Administrators' right to documents.

In **Tiger v. Barclays Bank, Ltd.** (1951, W.N. 342), the bank had been named as executors under a will, which was disputed by T. The bank were appointed administrators *pendente lite*. The action was subsequently the subject of a compromise under the terms of which the bank renounced probate and T. was granted letters of administration. T. then demanded that the bank should hand over all the documents relating to the estate but the bank refused to do this until they had been given a formal release from all liability in respect of the estate; they contended that there was an implied term to this effect in the compromise. Finnemore, J., rejected this contention and held that T. was entitled to the documents unconditionally.

Negligence—Fall caused by defective sash window.

It has always seemed remarkable to the writer that more accidents do not occur to window-cleaners, as they balance themselves on narrow sills with nothing but the window sashes to afford a handhold. In **Christmas v. General Cleaning Contractors and others** (1951, W.N. 294), one window-cleaner had been unlucky. He was holding on to one sash window when the other came down and knocked his fingers away, causing him to fall nearly thirty feet to the ground. He sued both his employers and the club whose windows he was cleaning. The Court held both defendants liable—the employers because they had failed to provide a safe system of working and the club because as invitors they had a duty to take reasonable care to guard against unusual dangers and they had failed in this duty by not having the windows inspected from time to time.

Bankruptcy—Rights of execution creditor against trustee.

On September 8, 1949, L. committed an act of bankruptcy; on November 8 a petition was presented; on December 4 a receiving order was made and on January 5, 1950, he was adjudicated bankrupt in the High Court. Meanwhile, on October 4, 1949, a County Court judge had fined L. £10 for contempt of Court; under a warrant of execution, dated October 17, the Registrar seized L.'s furniture on November 4 and sold it on November 15, keeping £10 out of the proceeds to satisfy the fine; the Registrar had no notice of the act of bankruptcy or of the presentation of the petition.

The trustee in bankruptcy claimed that, as his title related back to the date of bankruptcy under Section 37 of the Bankruptcy Act, 1914, the goods at the date of seizure must be treated in law as being his property and therefore the seizure was wrongful. The Registrar contended that he was protected by Section 40 (1), which provides that, where a creditor has issued execution, he shall not be entitled to retain the benefit of the execution against the trustee in bankruptcy unless he has completed the execution before the date of the receiving order and before notice of any available act of bankruptcy or of the

presentation of a petition. It will be noticed that these provisions do not expressly give the execution creditor a right to retain the benefit if he has executed in time: they merely say that he shall not have the benefit if the execution is not completed in time. The question therefore for Danckwertz, J., in **re Love** (1951, 2 A.E.R., 321) was whether Section 40 (1) was merely "restrictive" of the execution creditor's rights or whether it positively "protected" those rights. The learned Judge held that the Section was protective and that as the registrar had completed the execution in time he was entitled to retain the £10.

This affirms the view of the law formerly held by nearly all practitioners.

Local Government—Duty of auditors to surcharge for negligence.

Two ratepayers of a borough council discovered that certain building work was being badly done by contractors to the council. The matter was reported to the council and, after an inquiry, the contractors made good some defective work. The ratepayers were still dissatisfied on the ground that payments had been made for other work which had not been properly done and which had not been put right: they asked the District Auditor to surcharge the council or its officials because, if proper supervision had been exercised, either the payments would not have been made or the works would have been put right by the contractor. The District Auditor heard evidence and refused to make a surcharge: he ended his decision by saying:

> There have been isolated instances of defective work which have escaped the notice of the council's officers, but they do not appear to me to have been of an extent or of such frequent occurrence as to warrant my finding that, but for gross negligence on the part of the officers, they would have been brought to light.

By Section 228 (1) of the Local Government Act, 1933:

> It shall be the duty of the District Auditor . . . to surcharge the amount of any loss or deficiency upon the person by whose negligence or misconduct the loss of deficiency has been incurred.

and in their appeal to the Divisional Court (**Pentecost v. London District Auditor** (1951, 2 A.E.R., 330), the ratepayers contended that in referring to "gross negligence" the District Auditor had applied the wrong test. The Court said that, except in criminal cases, epithets applied to negligence are meaningless so far as the common law is concerned; a man is either guilty of negligence or he is not. The fact that the word "negligence" in the Section was used with the word "misconduct" did not mean that the negligence must involve moral culpability or be what is sometimes called "gross negligence": *dicta* to the contrary in *Davies* v. *Cowperthwaite* (1938, 2 A.E.R., 685) were wrong. The District Auditor had therefore used the wrong phrase but, as his decision taken as a whole showed that he had found no negligence in the council's officers, his decision was right and would stand.

Compensation for gas companies.

The case of **Studholme v. Minister of Fuel and Power** (1951, 2 A.E.R., 371) lays down certain principles on which unquoted securities are to be assessed for compensation under the Gas Act, 1948. Those concerned with such assessments should study the full report.

THE SOCIETY OF Incorporated Accountants

RESULTS OF EXAMINATION IN SOUTH AFRICA

FINAL EXAMINATION, MAY, 1951

Candidates Passed (28)

ADAMS, William Patrick Charles Baddeley (with Goldby, Panchaud & Webber, Johannesburg); BLERSCH, Michael (with Jack Bobrov, Levien & Co., Cape Town); BOWLEY, Brian Allan (with J. E. P. Close & Co., Cape Town); BULL, Hugh Morgan (with Deloitte, Plender, Griffiths, Annan & Co., Johannesburg); BULLIVANT, Harold (Douglas, Low & Co., Johannesburg); CATCHPOLE, Alan Michael (with Charles Hewitt & Co., Johannesburg); CHAPLIN, Charles Michael Tunstall (with Douglas, Low & Co., Cape Town); CULLINGWORTH, Roy Brisbane (with Allan & Harsant, Salisbury); DU MÉE, Paul René de Chasteigner (with Deloitte, Plender, Griffiths, Annan & Co., Cape Town); FORBES, James (with Pulbrook, Wright and Underwood, Salisbury); FRANK, Selwyn Boris (with K. Sandler, Cape Town); GEELING, Kenneth Granville (with Wolpert & Abrahams, Durban); HARGREAVES, Eric (with George Mackeurtan, Son & Crosoer, Durban); HOLTMAN, Colin (with A. C. Sargeant & Jones, Cape Town); IRWIN, Oliver John (with Deloitte, Plender, Griffiths, Annan & Co., Ndola); LATHAM, Patrick (with Deloitte, Plender, Griffiths, Annan & Co., Johannesburg); LEVIEUX, Jean Frank (with Wackrill & Anderson, Johannesburg); LEVINKIND, Julius (with Jack Bobrov, Levien & Co., Cape Town); MACINTOSH, Roderick Graham (with Goldby, Panchaud & Webber, Johannesburg); MILLER, Alec (with Jack Bobrov, Levien & Co., Cape Town); MORGAN, Peter (with Goldby, Panchaud & Webber, Johannesburg); MORLEY, Douglas Stuart (with J. E. P. Close & Co., Cape Town); ORCHARD, Stanley Vernon (with Gibson, Hyslop & Winearls, Cape Town); RALPHS, Derek Vincent (with Dix, Boyes & Co., Pietermaritzburg); SCOTT, Graham Killoh (with Douglas, Low & Co., Cape Town); TENNICK, William Herbert (with Wolpert & Abrahams, Durban); WEINBERG, Basil Richard (with K. Sandler, Cape Town); WOOD, Robert Jackson (with Gibson, Hyslop & Winearls, Cape Town).

(*Eleven candidates failed to satisfy the examiners.*)

EVENTS OF THE MONTH

SEPTEMBER 8, 15, 22
Liverpool: "Accounting" (Intermediate), by Mr. V. R. Anderson, at 9.30 a.m. "Advanced Accounts" (Final), by Mr. V. R. Anderson, at 11 a.m.

SEPTEMBER 13 TO 18
Cambridge: Incorporated Accountants' Course at Gonville and Caius College.

SEPTEMBER 24 TO 28
London: Pre-examination courses at King's College. Arranged by Students' Society.

SEPTEMBER 29
Liverpool: "Executorship" (Intermediate), by Mr. W. A. Kieran,, A.S.A.A., at 9.30 a.m. "Taxation" (Final) by an Inspector of Taxes, at 11 a.m.

COUNCIL MEETING

JULY 19, 1951

Present: MR. C. PERCY BARROWCLIFF (President), Mr. Bertram Nelson (Vice-President), Sir Frederick Alban, Mr. A. Stuart Allen, Mr. Edward Baldry, Mr. R. Wilson Bartlett, Mr. H. J. Bicker, Mr. F. Sewell Bray, Mr. Henry Brown, Mr. M. J. Faulks, Mr. Alex. Hannah, Mr. C. A. G. Hewson, Mr. H. O. Johnson, Mr. A. E. Middleton, Mr. T. H. Nicholson, Mr. James Paterson, Mr. F. A. Prior, Miss P. E. M. Ridgway, Mr. P. G. S. Ritchie, Mr. R. E. Starkie, Mr. Percy Toothill, Mr. Richard A. Witty, Sir Richard Yeabsley, with the Secretary, the Deputy Secretary and the Assistant Secretary.

COUNCIL

The resignations from membership of the Council of Mr. R. M. Branson, Mr. Walter Holman and Mr. T. Harold Platts were received with much regret. The Council expressed its warm appreciation of the services rendered by each of these three members over a long period of years.

REPORTS OF COMMITTEES

Reports were received of recent meetings of the Applications, Development, Disciplinary, District Societies, Dublin Conference, Examination and Membership, and Finance and General Purposes Committees, of the Board of Examiners, and of the ACCOUNTANCY Editorial Conference.

MANAGEMENT ACCOUNTING

Approval in principle was given to the holding of a course at Ashridge during 1952 on Management Accounting.

UNITED STATES AND CANADA

Mr. T. H. Nicholson reported that during a recent visit to the United States of America and to Canada he had had conversations with members of the profession in New York, Toronto and Montreal.

It was reported that the American Institute of Accountants had invited the President and Secretary of the Society to attend the sixty-fourth annual meeting of the American Institute, to be held at Atlantic City, New Jersey, from October 6 to 10, 1951. The invitations had been regretfully declined owing to engagements in this country.

The President had similarly been obliged to decline an invitation to attend the forty-ninth annual general meeting of the Canadian Institute of Chartered Accountants in Banff, Alberta, from September 3 to 6, 1951.

SCOTTISH BRANCH

The Council approved the alteration of the rules of the Scottish Branch to render Associates as well as Fellows eligible for election to the Scottish Council.

DUBLIN CONFERENCE

The Council recorded its gratitude to the President and members of the Council of the Irish Branch for the excellent arrangements made for the Conference held at Dublin from June 13 to 16; and to all members of the Irish Branch and of the Belfast and District Society for the generous hospitality shown to members of the Society who visited Dublin.

INSTITUTE OF CHARTERED ACCOUNTANTS OF SCOTLAND

Upon a report by the President on the completion of the amalgamation of the three Scottish bodies, the Council adopted a resolution of congratulations to the newly-established Institute of Chartered Accountants of Scotland and to its first President, Mr. R. G. Simpson.

SOUTH AFRICAN BRANCHES

The Council received the minutes of recent meetings of the Committees of the three branches in South Africa, and of the twenty-fifth annual general meeting of the Western Branch.

It was reported that the Accountancy Bill had now been passed by the Union Parliament.

DEATHS

The Council received with regret a report of the death of each of the following members: Atkins, Joshua Ralph (Fellow), Manchester; Bhatia, Prithvi Nath, B.COM. (Associate), Calcutta; Chater, Thomas Farey (Associate), Kettering; Greenwood, Frank Goldthorp (Associate), Halifax; Hicks, Elijah Bertie (Associate), Weston-super-Mare; Howard, Frank (Fellow), London; Levy, Ise (Fellow), Cape Town; Shackleton, Max Stanley (Associate), Brighouse; Shand, David (Fellow), Sydney; Statham, Edgar (Associate), Stoke-on-Trent; Wakeling, Charles Edward, J.P. (Fellow), London.

DISTRICT SOCIETIES

LONDON STUDENTS' SOCIETY

CRICKET MATCH

THE CRICKET MATCH BETWEEN THE MEMBERS of the Chartered Accountants Students Society of London and the Incorporated Accountants Students Society of London, played on the Barnet Cricket Ground on August 15, produced a most exciting finish. With eight minutes left to play and with the last man in, the Chartered Students required 35 runs to win. The batsmen, however, defied all the bowlers' attempts to force a win, and the match ended in a draw. This was the third match between these two Students' Societies, of which the Incorporated Students won the first two. *Scores:*

Incorporated Students of London

G. P. Laxton, c. Ravenscroft, b. Ezekiel	43
J. T. D'Eath, run out	77
V. Lyall, st. Laws, b. Rata	2
K. G. Taylor (capt.), l.b.w., b. Ezekiel	18
J. A. Cornfield, run out	5
A. H. Smith, l.b.w., b. House	1
J. E. O'Flynn, c. House, b. Rata	37
L. A. Warren, st. Laws, b. Rata	14
N. Lloyd, b. Rata	0
W. R. McBrien, b. Rata	0
E. T. Allen, not out	0
Extras: nil	
Total	197

Bowling: V. A. Ravenscroft 4-0-33-0. H. Colin-Thomé 12-0-64-0. D. Rata 12-0-59-5. D. Ezekiel 8-1-32-2. M. House 4-0-9-1.

Chartered Students of London

M. House, l.b.w., b. Warren	6
H. Colin-Thomé, c. and b. Warren	3
D. T. H. Nicholson, run out	5
M. L. Laws, run out	19
B. D. Barton (capt.) c. Lyall, b. Taylor	46
D. Ezekiel, b. Allen	0
A. G. Stoughton-Harris, st. Laxton, b. O'Flynn	7
D. Rata, not out	58
G. J. Cooper, l.b.w., b. Warren	1
V. A. Ravenscroft, c. Allen, b. Taylor	9
J. G. Winn, not out	0
Extras: b. 4, l.b. 4	8
Total (9 wickets)	162

Bowling: N. Lloyd 11-4-34-0. L. A. Warren 12-0-44-3. E. T. Allen, 6-0-19-1. J. E. O'Flynn 6-1-29-1. V. Lyall 2-0-14-0. K. G. Taylor 4-1-14-2.

LEICESTER

ANNUAL REPORT

SEVEN MEETINGS WERE HELD IN LEICESTER and five in Northampton, most of them in collaboration with other bodies.

The Students' Section held an enjoyable dance; it has been decided to make this an annual event. The Students' Cricket Club again had an active season. Pre-examination lectures were given, and ten lectures were arranged jointly with the Leicester Chartered Accountants' Students' Society.

The District Society now has 214 members and 203 students.

Congratulations are extended to ten Final and eighteen Intermediate candidates who were successful in their examinations.

The Research and Taxation Sub-Committees at Leicester and Northampton had an active year and have done useful work.

The hon. secretary has been appointed to represent the District Society on the Council of the Chamber of Commerce.

A successful informal meeting was held with the Inland Revenue at which a number of matters of mutual interest were discussed.

MANCHESTER

MR. ARTHUR T. EAVES HAS BEEN ELECTED president in succession to the late Mr. G. W. Street, whose regretted death was recorded in our last issue. Mr. Victor A. Bell is the new vice-president, and Mr. Frank O. Wilson hon. treasurer.

NOTTINGHAM, DERBY & LINCOLN

THE FORTY-SECOND ANNUAL MEETING WAS held on July 25, preceded by a luncheon, and was well attended. The president, Mr. C. F. Carlisle, F.S.A.A., was in the chair.

The following officers were elected: President, Mr. P. W. Skinner, F.S.A.A.; vice-president, Mr. H. F. Ingram, A.S.A.A.; honorary secretary and treasurer, Mr. C. M. Foxon, F.S.A.A.

PERSONAL NOTES

Mr. S. A. Spofforth, F.C.A., F.S.A.A., has been elected president of the Institute of Taxation. The vice-presidents are now Mr. C. Gordon Howard, B.A., and Mr. James Wood, A.C.A.

Mr. Ernest Long, F.S.A.A., has been appointed secretary to the British Electricity Authority.

Messrs. Geo. Mackenzie & Co., Chartered Accountants, Johannesburg, have opened a branch office at Kilmarnock Buildings, Corner Eleventh Avenue and Fife Street, Bulawayo, Southern Rhodesia. P.O. Box 238.

Mr. E. H. Richardson, A.S.A.A., has commenced public practice under the style of Richardson & Co., Incorporated Accountants, at Regal Chambers, High Street, Shanklin, Isle of Wight.

Mr. Frank Haynes, F.S.A.A., Leicester and Lutterworth, has taken into partnership Mr. K. J. Moulsher, A.S.A.A., and Mr. D. I. Sharman, who have been associated with him for a number of years. The firm name will remain Frank Haynes & Co.

Mr. J. Ghosh, M.A., A.C.A., A.S.A.A., has commenced public practice at 10, Old Post Office Street, Calcutta, 1.

Mr. T. P. E. Campbell, Incorporated Accountant, has commenced public practice at Avenida dos Aliados, 20-4, Porto, Portugal.

Mr. K. T. Wood, A.S.A.A., has commenced public practice as a partner in Messrs. Derry, Ellman-Brown & Fraser, Bain Bros. Buildings, P.O. Box 702, Salisbury, Southern Rhodesia.

Messrs. Walter Bell & Co., Sheffield, have taken into partnership Mr. Geoffrey Ridal, A.S.A.A.

Messrs. Francis Dix, Bird & Co., Johannesburg, have admitted to partnership Mr. B. E. J. Blann, B.COM., A.S.A.A.

Mr. Norman Griffiths, F.S.A.A., has retired owing to ill-health from partnership in the firm of E. B. Griffiths & Co., Southport. The practice is being continued by the remaining partners, Mr. A. H. Griffiths and Mr. T. H. Sutton, F.S.A.A., under the style of Griffiths & Sutton.

Messrs. Goldby, Panchaud & Webber, Incorporated Accountants, Johannesburg, have taken into partnership Mr. H. C. Twycross, A.S.A.A.

By mutual consent the partnership between Mr. P. D. Pascho, Mr. S. G. T. Holmes and Mr. G. Dudman has terminated. Mr. Pascho and Mr. Dudman are continuing to practise under the style of Roberts & Pascho, Incorporated Accountants, at 2, Ermington Terrace, Mutley Plain, Plymouth. Mr. Holmes is now practising as Gerald Holmes and Co., Incorporated Accountants, at 1, Seaton Avenue, Mutley, Plymouth. His telephone number is Plymouth 5806.

Mr. J. H. Rock, Incorporated Accountant, has commenced public practice at Lombard House, Great Charles Street, Birmingham, 3.

Mr. A. Hopper, Incorporated Accountant, has commenced public practice at 9, High Row, Darlington.

REMOVALS

Messrs. S. V. Ghatalia & Co. have removed to Dhun Building, Nanabhoy Lane, Flora Fountain, Fort, Bombay.

Messrs. Walton, Watts & Co., Chartered Accountants, have removed to Chancery Chambers, 55, Brown Street, Manchester, 2.

Mr. A. J. Shah, B.COM., G.D.A., A.S.A.A., practising as A. J. Shah & Co., advises a change of address to 70, Medows Street, Fort, Bombay.

OBITUARY

JOHN PERCIVAL DUXBURY

We learn with much regret that Mr. J. P. Duxbury, F.S.A.A., died on July 11, at the age of 62. Mr. Duxbury was the senior partner of Messrs. Nathaniel Duxbury, Son & Co., Blackburn. He became a member of the Society in 1911, and entered into partnership with his father, the late Mr. Nathaniel Duxbury, F.S.A.A., who had been President of the Manchester District Society and subsequently a founder member of the Committee of the North Lancashire District Society. Mr. J. P. Duxbury served on the North Lancashire Committee from 1931 to 1942. He was a Freemason and a member of Blackburn Conservative Club.

FREDERICK DALL GRAY

It is with much regret that we announce the sudden death on July 18 of Mr. Frederick Dall Gray, F.S.A.A., senior partner of Messrs. Frederick Dall Gray & Co., Coleraine and Belfast. He was 56 years of age. He qualified as an Incorporated Accountant in 1928 and in 1934 commenced public practice as a partner in Messrs. Lawther, Bass & Co., with whom he had already been associated for a number of years. He was also a Fellow of the Institute of Taxation.

Mr. Gray was a prominent Freemason, being a P.M. of Vernon Lodge 127, Coleraine. He was a member of Portstewart Golf Club, and was formerly a keen player of hockey and cricket.

ARTHUR REGINALD GREEN

We regret to record the death on July 12, as the result of an accident, of Mr. A. R. Green, F.S.A.A., senior partner in Messrs. Arthur E. Green & Co., Incorporated Accountants, London, E.C.2. He became a member of the Society of Incorporated Accountants in 1906, after taking Honours at the Final Examination, and was admitted to partnership in the firm in 1911.

JAMES HENSHALL

We regret to record that Mr. James Henshall, F.C.A., A.S.A.A., died on August 1, at the age of 79. He became a member of the Society of Incorporated Accountants in 1895, when he was in the service of Messrs. J. E. Edwards, Son & Warmsley, Chester. He was admitted to partnership in 1905, and in the same year became a member of the Institute of Chartered Accountants. He subsequently became senior partner in the firm, now known as Warmsley, Henshall and Co.

Mr. Henshall was widely known in Chester, where he had held many directorships and other appointments, including the chairmanship of Chester Boat Co., Ltd., and of the Dee Steam and Motor Boat Co., Ltd. He had been treasurer of Chester Diocesan Training College. He was formerly a keen player of cricket, football and hockey.

The funeral service took place at St. John's Church, Chester, on August 4.